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Environmental, Social, and Governance Risk and Performance: Implications for Audit and Corporate Governance Research

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Jenna J. Burke

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DEDICATION

To my father, David Burke, for his unceasing support and for teaching me the importance of hard work.

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ABSTRACT

Environmental, Social, and Governance Risk and Performance: Implications for Audit and Corporate Governance Research

Jenna J. Burke

Chair of the Supervisory Committee:
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This dissertation examines oversight of environmental, social, and governance (ESG) related risk and performance. These considerations are a new piece of business language, and are crucial in monitoring and evaluating the sustainable impact of modern corporations. The dissertation is comprised of three archival studies, which together contribute to an emerging accounting literature at the intersection of audit and corporate governance.

The first study uses hand-collected data on voluntary board-level committees that oversee ESG-related issues to investigate the performance implications of these committees. This paper presents a theoretical framework and methodology that incorporate the committee's role in shared value creation and the heterogeneity of ESG-related issues. When this theoretical and methodological approach is applied, I find that committees with ESG-related responsibilities do have positive performance implications.

The second and third studies use a new dataset to explore accounting-related consequences of negative media coverage of ESG practices. In the second study, I find that when audit client reputation is damaged via negative media coverage, auditors respond to protect against reputation loss spillovers. Specifically, results suggest that auditors avoid undue reputation risk by resigning from engagements and reduce/share undue risk by

charging higher audit fees. This study is important because it documents auditor oversight of, and response to, ESG-related risks. Further, the study answers recent calls for U.S. evidence of auditor reputation risk as a component of auditors' risk considerations.

Finally, in the third study, I investigate whether corporate boards hold CEOs publicly accountable for negative media coverage of ESG practices. Understanding board sensitivity to ESG issues, measured by their turnover decisions, is important given a rising demand for sustainable business practices. Findings of this study suggest that when ESG issues are highly publicized, CEO dismissal likelihood is higher. Overall, findings support both the importance of these issues to modern corporations and the monitoring role of the media.

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Part One

The Heterogeneity of Board-Level Sustainability Committees and Corporate Social Performance

Citation: Burke, J. J., R. Hoitash, and U. Hoitash. 2017. The heterogeneity of board-level sustainability committees and corporate social performance. *Journal of Business Ethics*, forthcoming.

I. INTRODUCTION

Modern corporations and their boards face new oversight responsibilities as managing stakeholder interests becomes an essential component of running an ethical for-profit organization. Sustainability risk management has also become crucial, as business strategy now must ensure that sustainability policies and impacts do not deflect from achievement of primary business objectives (COSO 2013). One primary mechanism to integrate these considerations is through specialized sustainability committees at the board level. These committees oversee impacts on the community, employees, the environment, consumers, suppliers, and more. Such committees have become increasingly prevalent, representing a shift towards stakeholder (i.e. any group who affect, or are affected by, a company's operations) accountability and the creation of shared value at the highest level of firm governance (Porter and Kramer 2011; The Conference Board, 2010; The Corporate Library, 2010). Presumably, this formal accountability to stakeholder groups is a substantive oversight mechanism.

Surprisingly, the extant literature finds little evidence of an impact of sustainability committees on performance outcomes (Al-Tuwaijiri et al. 2004; Berrone and Gomez-Mejia, 2009; Mallin et al. 2013; Rodrigue et al. 2013; Walls et al. 2012). For example, Rodrigue et al. (2013) and Berrone and Gomez-Mejia (2009) detect no association between these committees and environmental performance or environmental metrics in executive compensation, respectively. This finding is puzzling and inconsistent with the finding that high sustainability companies adopt such a committee (Eccles et al., 2014) and the findings of broader corporate governance literature that governance via committee specialization influences corporate outcomes (e.g., Beasley, 1996; Klein, 1998; Singh and Harianto,

1989; Uzun et al. 2004). Gaining a better understanding of this new board composition feature and its performance is an important practical endeavor.

Our first objective is to examine the existence of these committees and offer a framework through which their contribution to sustainability performance can be investigated. In doing so, we theorize that sustainability committees are a mechanism to create shared value (Porter and Kramer 2011), where the interests of a diverse group of stakeholders is satisfied and sufficient profit is achieved (Lopez et al. 2007). This approach is evident in several of the responsibility statements of sustainability committees that we analyze in this manuscript, which address stakeholder expectations while prioritizing economic success. To create shared value, sustainability committees manage opportunities and risks to pursue positive sustainability performance and to limit the impact of negative sustainability performance. Importantly, we hypothesize that a sustainability committee may not have a consistent impact on both of these performance indicators. We predict that a sustainability committee contributes to positive indicators such as giving to charities or adopting environmentally friendly policies, which generate value to both shareholders and stakeholders. For negative indicators, such as lending practices that have led to controversies or environmental pollution, we caution that certain risks may be inherent to a company's operations and that a sustainability committee may rather serve as a high-level control mechanism to protect value by managing risk, and its resulting impact will depend on the company's risk appetite.

To test these hypotheses, we use corporate social performance (CSP) strengths and concerns data from MSCI ESG STATS to proxy for positive and negative performance indicators, respectively. We find that a sustainability committee has a positive impact on

both CSP strengths and concerns, which is consistent with the committee generating value from opportunities and protecting value from risks. The latter result is possibly driven by companies that inherently have greater sustainability concerns and adopt committees to monitor the impact of these concerns on shared value. For these companies, fully mitigating concerns may be difficult or value-destroying. Prior literature examining sustainability committees has not considered these important conceptual and empirical differences between positive and negative sustainability performance.

Our second objective is to explore the diverse range of stakeholder impacts that a sustainability committee oversees, which prior literature has not considered. For instance, research often uses the term "environmental committee" to refer to a broad scope of committees that focus on not only environmental issues, but also those that have general names such as "public policy," "public affairs," and "corporate responsibility" (e.g., Rodrigue et al. 2013). Aggregating committees in this way may explain why consistent associations with relevant performance outcomes have not been detected. In reality, sustainability is a multi-faceted construct that encompasses a firm's environmental and social impacts. As might be expected when voluntary sustainability committees are formed, responsibilities differ greatly from one company to another. These committees are a formal acknowledgement of responsibility to specific stakeholder groups, which enhances accountability (i.e., the expectation that one may be called upon to justify one's actions to others) and acts as a goal to affect action and strengthen the performance impact for those stakeholders (Dubnick 2005; Ryan and Smith 1954). For example, committees that focus on the environment are theoretically and practically likely to influence different actions and performance outcomes than committees that focus on employee-related issues. Further,

some committees may focus on a single stakeholder, while others focus on many stakeholders and must balance these competing interests. Treating these heterogeneous committees equally can lead to incorrect inferences from empirical analysis.

To achieve this second objective, we offer a methodology rooted in accountability and goal setting theories for measuring sustainability committee existence and focus. Specifically, we hand collect sustainability committee responsibility disclosures from public company proxy filings of U.S. firms for the period 2003 – 2013. Within these 1,243 disclosures, firms explicitly claim accountability for oversight of four stakeholder groups (i.e., community, employee, environment and consumer/supplier). We combine this hand-collected data with publicly available data on committee characteristics. To the best of our knowledge, our study provides the first comprehensive examination of the existence and focus of sustainability committees within a large sample of public companies. Guided by accountability and goal setting theories, we argue that research can be improved by evaluating the effectiveness of committees that focus on a specific stakeholder based on their performance along that dimension. We also predict that, beyond stakeholder focus, sustainability committees are heterogeneous in their effectiveness due to resource availability. We perform univariate analysis to examine how committee size, independence, and meeting frequency are associated with performance variation within the committee sample and each group of focused committees.

Empirically, we use CSP data from MSCI ESG STATS to test these predictions. Griffin and Mahon (1997) state "collapsing the KLD's [MSCI] multiple dimensions into a unidimensional index may mask the individual dimensions that are especially important and relevant for a specific company or industry". We address this critique with our

aforementioned disaggregated performance analysis. Further, we address the critique of industry heterogeneity by recognizing that a cross-sectional analysis within the entire sample may not appropriately capture the industry-specific nature of CSP. For example, committee focus and effectiveness will likely differ between the *Oil and Gas Extraction* and *Retail* industries. We thus present a quantitative approach to classifying industries based on their sensitivity to different stakeholder groups using the four dimensions of CSP in MSCI: *Community, Employee, Environment and Consumer/Supplier*. These two disaggregation techniques, analyzing CSP by dimension and within industries sensitive to certain stakeholder groups, contribute to our goal of drawing reliable conclusions on the impact of sustainability committees on performance.

In sum, we contribute to the literature by presenting a comprehensive examination of sustainability committee existence and focus. These committees are becoming increasingly prevalent, and are mechanisms to create shared value for stakeholders and shareholders. We offer a method to classify committee responsibilities, which generates interesting descriptive statistics that help emphasize the heterogeneity of committee responsibilities and will aid future research in understanding sustainability oversight practices at these institutions. We conduct our analysis by a) separately examining positive and negative sustainability performance outcomes, b) pairing committee stakeholder focus with the relevant performance outcome, and c) isolating the sample to relevant sensitive industries. These methods of disaggregation resulted in empirical findings that are consistent with theory. These findings suggest that board-level sustainability committees focused on specific stakeholder groups have performance implications in that stakeholder dimension, which supports accountability theory. We generally find that sustainability

committees positively influence sustainability strengths, but do not mitigate concerns. These associations are consistent with our overarching theory that sustainability committees contribute to shared value creation, where they both generate value by pursuing strengths and protect value by monitoring, but not necessarily mitigating, concerns. Further, in univariate tests of additional committee characteristics we find that if boards don't dedicate the proper resources to these committees, even focused sustainability committees can fail to enhance performance.

Overall, we provide evidence for a more nuanced understanding of the performance impact of sustainability committees. This evidence should prove useful for both practitioners and future research. Practically, we provide evidence that stakeholders can gauge committee effectiveness from the information published in proxy filings (e.g., committee focus, industry alignment, size, independence, and meeting frequency). Future research can follow a similar method in other sustainability-related contexts.

II. BACKGROUND ON SUSTAINABILITY COMMITTEES

As awareness of key stakeholder relations rises, many firms have restructured their traditional corporate governance structure to include a committee to manage stakeholder oversight demands (The Conference Board, 2010; The Corporate Library, 2010). Firms voluntarily adopt these board-level committees in addition to the principal audit, compensation and nominating committees mandated by the major US stock exchanges. Recent practitioner publications have examined the prevalence of sustainability related committees, reporting that 65 percent of the S&P 100 firms and nearly one-fifth of the Russell 1000 have such a committee. These committees are most frequently found in

industries that are classified as environmentally sensitive (The Corporate Library, 2010).[1] Committee duties span from a general focus on overall sustainability policies and procedures to specific foci on stakeholder groups such as employees or the environment. Since these committees are voluntary, a board can dictate which stakeholder groups they focus on. For example, in 2013, Arch Coal, Inc. had an "Energy and Environmental Policy" committee, which focused on compliance with emerging environmental policy. Delta Air Lines Inc. had a "Safety and Security" committee in the same year, which focused on ensuring the safety of the airline's employees and passengers. While the responsibilities of these committees are vastly different, both are forms of stakeholder oversight and represent the extension of corporate accountability to non-shareholder stakeholder groups.[2] Therefore, we define a sustainability committee as the extension of governance to the impacts of the business on various stakeholder groups – these stakeholder groups include: the community, employees, the environment, consumers, and suppliers.

There is limited research on voluntary board-level sustainability committee as an element of board structure. Ostensibly, the existence of these committees is a formal and visible commitment to stakeholders, making concrete the relationship between corporate governance and sustainability. While broader corporate governance research consistently finds positive performance implications of board-level committees (Baxter et al., 2013; Beasley, 1996; Beasley et al., 2000; Conyon and Peck, 1998; Klein, 1998; Singh and

[1] Of note is that previous academic literature has used the term "environmental committee" and other general terms to describe the very same classification. We use the term "sustainability" as the descriptor throughout this study as it labels the committees most effectively as stakeholder related.

[2] Stakeholders are defined as those that have a legitimate stake or claim on the business (Donaldson and Preston, 1995) because they affect or are affected by the business (Freeman, 1984). These stakeholders range from customers to employees, suppliers, and the local community (Clarkson, 1995; Freeman, 1984). The increasing popularity of the voluntary board-level sustainability committee is important in reflecting the extent that stakeholder interests have been integrated into corporate decision-making (Luoma and Goodstein, 1999).

Harianto, 1989; Uzun et al. 2004)[3], findings for sustainability-related committees have been less consistent. Two studies that examine the direct association of environmental committee existence and performance outcomes have not detected significant associations (Berrone and Gomez-Mejia 2009; Rodrigue et al. 2013).

III. THEORETICAL DEVELOPMENT

Accountability theory

Voluntary governance at the board-level is unique in that a brief description of any formal committee responsibilities must be listed in the annual proxy filings. Explicitly listing responsibilities serves to establish and communicate the priority of these issues to external parties, and makes a company's intentions known to the relevant audience. In this way, the voluntary creation of sustainability committees is presumably a sign of accountability to stakeholder groups.

A person or group of persons is said to be accountable when they acknowledge and assume responsibility for actions, decisions, and policies within the scope of their role. Accountability refers to the implicit or explicit expectation that one may be called upon to justify one's beliefs, feelings, and actions to others (Lerner and Tetlock, 1999). Being held accountable motivates and triggers directors, and thus the committees they sit on, to do

[3] Prior research has examined the existence of several board-level committees and their direct impact on respective areas of responsibility. For instance, accounting research finds that before the requirement to have an audit committee, firms that voluntarily formed audit committees were generally found to have higher quality financial reporting processes and better external audit oversight (e.g., Beasley, 1996; Beasley et al., 2000). Further, extensive literature examines the performance outcomes of nominating and compensation committees (e.g., Conyon and Peck, 1998; Singh and Harianto, 1989; Uzun et al., 2004). While these three principal committees are now common on corporate boards, research continues to find that voluntary committees, such as the finance and investment committee or risk committee also have an impact on relevant outcomes (e.g., Baxter et al., 2013; Klein, 1998). Of note is that the Dodd-Frank Act now requires board-level risk committees for certain bank holding companies.

what they are tasked with or risk being punished for failures (Gilson, 1990; Srinivasan, 2005; Tetlock, 1983).

The means for stakeholders to hold a company accountable are often tied to their everyday actions related to the corporation. For instance, community stakeholders can choose whether or not to support local operations. Employees can influence a corporation through their employment choices. Representatives of the environment stakeholder can hold firms accountable through their votes on regulation affecting an industry. Consumers and suppliers can hold firms accountable through their purchases and offering behavior. Together, these stakeholder actions can influence reputation and impact overall firm value (Filbeck et al. 1997; Anderson and Smith 2006). This is particularly true in the current business environment where attention to sustainability is prevalent in the news media. Stakeholders can further raise attention to sustainability issues if they feel performance is inadequate. Recent anecdotes illustrate that sustainability issues can become detrimental to a company's primary business objectives. For instance, Volkswagen's emissions scandal (e.g., Russell et al. 2016, Vlasic and Chapman 2016) and Chipotle's food safety issues (Surowiecki 2015) are sustainability issues that have led to widespread negative media coverage and caused major business continuity concerns. This type of negative attention informally holds sustainability committee members accountable.

Shareholders are also a major stakeholder group and have the power to hold directors accountable through their voting rights and resolutions. Using unique data, recent shareholder voting literature has found that committee members are held accountable for the specific performance of the committees they sit on, making these members more effective (e.g., Gal-Or et al. 2016, Ertimur et al. 2012). Specific to sustainability issues,

shareholder activism is also on the rise, and the literature has found that even if these proposals do not receive a majority vote, they are effective at improving performance on the focal issue (Grewel et al. 2016). Thus, it's clear that sustainability issues such as caring for the environment and treating employees well are also desired and sometimes enforced by shareholders.

The expectation of being held accountable for one's responsibilities and actions results in an individual seeking to meet the perceived demands of the audience they are accountable to (Tetlock, 1991), increasing the probability of strong performance (Dubnick, 2005). In this way, the listed responsibilities of sustainability committees operate in the same way as goals, where direct attention to issues motivates effort towards that issue. Goal setting theory (Locke and Latham 1990) is closely aligned with the accountability arguments we set forth. Specifically, committee responsibilities act as conscious goals to affect action (Ryan and Smith 1954), strengthening the accountability to performance relationship.

Creating shared value

Recent literature has focused on "win-win" situations as motivation for company investment in sustainability (e.g., Ameer and Othman, 2012; Eccles et al., 2014; Laine, 2010; Lopez et al. 2007; Porter and Kramer, 2011). These situations are those which satisfy the aforementioned diverse group of stakeholders while also achieving sufficient profit (Lopez et al. 2007). Public corporations, who by law must protect shareholders' interests, have begun to recognize sustainability as a competitive advantage. While economic success and shareholder protection are the precondition for taking care of stakeholder responsibilities (Laine, 2010), the two are not opposing forces. Increasingly evident over

time is that sustainability and financial performance are often mutually beneficial, not exclusive (Ameer and Othman, 2012; Eccles et al., 2014). By addressing stakeholder needs that intersect with their business, companies can generate economic value (Porter and Kramer 2011). There are various means for economic value to be positively impacted when addressing stakeholder needs, including cost savings, employee retention, customer loyalty, regulatory compliance, gaining competitive advantage, revenue growth, innovation, and improvement in brand and reputation – all of which have a positive impact on the bottom line.

Within this approach to creating shared value, management is an important element influencing successful execution (Porter and Kramer, 2011). Specifically, boards can adopt committees and tailor their responsibilities in order to effectively develop opportunities and manage risks to generate and protect shareholder value, respectively (Kleffner et al., 2003; Beasley et al., 2005). The focus on shared value is evident in the responsibility statements of sustainability committees, which address stakeholder expectations while prioritizing economic success. For example, the following is an excerpt from the responsibility statement of Aflac's "Sustainability Committee":

> The Sustainability Committee assists management in setting strategy, establishing goals and integrating sustainability into the daily business activities of the Company's U.S. operation, including the formulation and implementation of policies, procedures and practices that permit the Company to respond to evolving public sentiment and government regulation in the areas of environmental stewardship, energy use, recycling and carbon emissions, that foster the sustainable growth of the Company's U.S. operations**.** *"Sustainable growth" means the ability to meet the needs of our shareholders and customers while taking into account the needs of future generations. "Sustainable growth" also equates to the long-term preservation and enhancement of the Company's financial, environmental, and social capital* [emphasis added].

Many other committees add a similar disclaimer, where attention to stakeholder issues is valued if they have an impact on operations, financial performance, or public image. These responsibilities make it clear that stakeholder needs are addressed with economic impact

in mind. Therefore, we theorize that this shared value consideration (Porter and Kramer 2011) motivates the existence of committees and the actions they take. While a sustainability committee is a formal sign of accountability to stakeholders, committees are unlikely to use resources to advance the interests of non-shareholder stakeholders if value is not created. Rather, a board-level sustainability committee serves as a formal mechanism to identify and prioritize sustainability issues based on their value importance, either by generating positive impacts or mitigating negative impacts.

Generating and protecting value

It is unreasonable to believe that a committee will uniformly value, prioritize, and impact sustainability-related opportunities and risks. For example, a committee may influence the action of adopting environmentally friendly policies, but may also allow firm operations to be a contributor to environmental harm (as seen in Aflac's Sustainability Committee responsibility statement). Sustainability opportunities can generate value, whereas risks can destroy value. A sustainability committee is likely to pursue sustainability-related opportunities that could enhance the firm's accountability towards stakeholders. At the same time, a sustainability committee will monitor lower-tail downside risks that could prove detrimental to firm value, and thus keep sustainability risks within the risk appetite of the organization. Companies are likely to have varying levels of both opportunities and risks, and committees are likely to have varying impacts on both as well. These opportunities and risks are realized in the form of positive and negative indicators of sustainability performance, commonly referred to corporate social performance (CSP) strengths and concerns, respectively.

Prior literature on sustainability committees has not always considered the conceptual differences between strengths and concerns, which is perhaps the explanation for inconsistent findings of a sustainability committee's impact (Rodrigue et al., 2013; Berrone and Gomez-Mejia, 2009). However, broader sustainability literature illustrates that the two are conceptually distinct constructs and that firms often simultaneously engage in responsible and irresponsible behavior (Mattingly and Berman, 2006; Strike et al., 2006; McGuire et al., 2003). For these reasons, it will prove important to separately predict a sustainability committee's impact on CSP strengths and concerns.

IV. HYPOTHESES

Aggregate performance impact of sustainability committees

Sustainability committee existence and CSP strengths

Corporate social performance (CSP) strengths include best practices concerning risks and opportunities related to the community, employees, diversity, the environment, human rights, and product dimensions of performance. These dimensions can be examined in aggregate and/or individually. For example, Walls et al. (2012) examine three board characteristics (committee existence, diversity, and board size) to determine how they combine to affect environmental performance of a company. Their study is one of the first to examine the link between corporate governance and environmental performance and finds significant associations between each element and environmental strengths. Extending this finding, Mallin et al. (2013) label the same board characteristics as evidence of stakeholder orientation and find that stakeholder orientation of the firm is positively associated with the people and product dimensions of CSP.

Guided by a shared value framework, a committee's impact on CSP strengths will depend on their ability to generate value. Strengths capture a company doing good and can generate value in a variety of ways, including their impact on employee retention, customer loyalty, revenue growth, improvement in reputation, and more. Aforementioned prior literature has shown sustainability investment to be positively associated with CSP strengths. Since the existence of sustainability committees can be considered such an investment, we make a directional prediction in our first hypothesis:

> **Hypothesis 1a:** The existence of a board-level sustainability committee is positively associated with CSP strengths.

Sustainability committee existence and CSP concerns

In addition to the aforementioned positive association between environmental committees and environmental strengths, Walls et al. (2012) also detect a positive association between environmental committees and environmental concerns. These findings are consistent with committees serving a risk management function. That is, companies that a-priori face greater sustainability risks are more likely to create sustainability committees.

The business environment today presents many challenges and potential risks to firms. For instance, a company may choose to oversee sustainability-related risks that are inherent to the company or industry including the risk of major detrimental events such as oil spills, product recalls, and occupational safety incidents. Effective management of sustainability risks does not necessarily imply that these risks are not or should not be taken by an entity, but rather it ensures that risk mitigating practices do not deflect from achievement of primary business objectives (COSO 2013).[4]

[4] Enterprise risk management is a crucial form of organizational governance, where companies aim to identify potential events that may affect the entity and manage risk to be within its risk appetite (COSO 2004).

In this way, a sustainability committee is a high-level control mechanism that assesses sustainability-related risks and evaluate their potential impact on achievement of primary business objectives. Once risks are assessed and understood, the decision on whether to take action to minimize risk will often depend on value considerations (Godfrey et al. 2009). Value is not generated if committee actions are not expected to sufficiently reduce costs associated with the resource investment or if the positive effects of risk reduction (e.g., reduced likelihood of negative events, reputation, sales, employee morale, etc.) are not material. Therefore, a committee that is focused on risk management may not generate positive performance implications for CSP concerns.

In sum, the prediction for the association between sustainability committees and CSP concerns is not without tension. It is possible that the dedication of board resources in the form of sustainability committees may lead to less concerns. In contrast, if sustainability committees are a risk control mechanism for firms with a-priori greater sustainability risks, then managing these risks may not result in less concerns. For this reason, we present the following hypothesis in non-directional form:

> **Hypothesis 1b:** The existence of a board-level sustainability committee is not associated with CSP concerns.

Heterogeneous performance impact of sustainability committee focus

Value considerations can also help prioritize corporate governance issues related to stakeholders by determining how resources should be allocated. The balancing of conflicting stakeholder interests can be difficult in practice and "rather than producing every kind of social value for every stakeholder, organizations find themselves constrained in practice by limited resources and bounded rationality, and thus tend to prioritize their stakeholders according to instrumental and/or normative considerations" (Jamali, 2008).

This suggests that certain stakeholder groups are prioritized differently amongst public companies according to their salience to the business model (Agle et al., 1999). Relatedly, specific goals are found to lead to higher performance (Locke et al. 1989). Specific responsibility statements remove ambiguity and allow a committee to focus on precise actions related to selected stakeholders, allowing performance to be more explicitly affected. For example, MGM Resorts "Corporate Social Responsibility Committee" focuses on the environment in its responsibility statement:

> The primary goal of our environmental sustainability initiative—the "Green Advantage"—is to reduce the impacts of our business on our natural environment. The premise of our Green Advantage is that environmentally responsible actions by us benefit our planet now and for the future, and result in more efficient operations, lower costs, and enhanced value.

However, the statement also mentions oversight of employee issues:

> The primary goals of our diversity and inclusion initiative include effective integration of diversity strategies into our major business functions and operations and promotion of an inclusive work environment and culture that are compatible with and respectful of the diversity of our employees, customers and business invitees, and that maximize employee engagement in accomplishment of our mission and business objectives.

Clearly, sustainability committees have heterogeneous foci which many not uniformly impact performance outcomes. Thus far, research on committees that oversee stakeholder interests has focused on the environmental dimension and detected little to no impact on environmental performance (Al-Tuwaijiri et al., 2004; Berrone and Gomez-Mejia, 2009; Mallin et al., 2013; Rodrigue et al., 2013). While these results are interpreted as environmental committees being primarily symbolic, we posit that the methodological choice to use an aggregate "environmental" committee construct may obfuscate the findings. In fact, these studies have included committees that seemingly have little environment related focus (e.g., public policy, sustainability, corporate responsibility).[5]

[5] For example, a public policy committee would be included in the Rodrigue et al. (2013) sample as an environmental committee, but could quite possibly have no environmental focus, leading to a measurement error that could explain the lack of significant results.

Given the increasing popularity of these committees in public companies, it is important to clarify their outcome effectiveness. While perhaps appropriate for previous research questions, the typical approach to associating sustainability committees and/or CSP in aggregate does not allow a distinction between committees that are accountable to and generate value from different stakeholders (Berrone and Gomez-Mejia, 2009; Mallin et al., 2013; Rodrigue et al., 2013; Walls et al., 2012). Committees may focus on a single stakeholder group or multiple stakeholder groups (e.g., the community and employees). The oversight of one stakeholder group likely requires different decisions than the oversight of another group, and may cause variation in outcome effectiveness. These decisions may also have varying impacts on value. For instance, how a firm manages its employees can lower turnover, improve productivity, and increase worker commitment, whereas positive consumer perceptions about product quality and safety can lead to increased sales and decreased costs (Berman et al., 1999).

For our purposes of comprehensively examining the impact of sustainability committees on CSP, we argue that committees hold heterogeneous responsibilities and warrant a more granular examination. We predict the performance implications of this in the following hypothesis:

> **Hypothesis 2:** A board-level committee with accountability towards specific stakeholders will have a stronger positive association with CSP performance in that dimension, relative to companies without a sustainability committee or those with a committee that is not focused on that dimension.

V. METHODS

Sample and data

We collect performance data from MSCI ESG STATS (formerly KLD)[6], which is merged with hand-collected data on the presence and responsibilities of board-level sustainability committees. We merge this data with Compustat and IRRC to obtain financial performance and governance characteristics data. The resulting sample includes a total of 11,458 firm-year observations with available data for all variables for the period 2003 – 2013. Table 1,1 displays information on the sample, including sample attrition and sample distribution by year. The sample increases over time, and by 2013 it includes data for 1,103 U.S. companies. Across all years, 1,742 unique companies are included in the sample.

[INSERT TABLE 1.1 HERE]

Variables and analysis

Dependent variables

We use various CSP measures as dependent variables in our empirical specifications. These measures are all constructed from the MSCI database, which provides data on six major dimensions of social performance (i.e. community, diversity, employee relations, environment, human rights, and product) that are commonly used to construct overall CSP measures (Hillman and Keim, 2001).[7] Following prior literature, we do not include the corporate governance dimension as it is considered distinct from CSP (Servaes and Tamayo, 2013). We create two measures of aggregate sustainability performance by

[6] The MSCI ESG STATS database assesses firms' CSP across a range of dimensions geared towards institutional investors (Sharfman, 1996). The database covers the largest 3,000 U.S. publicly traded companies by market capitalization, which includes both the S&P 500 and the MSCI KLD 400 Social Index. Data on CSP is collected from publicly available industry and company reports.

[7] Within the database, public companies are rated on approximately 60 indicators across seven major environmental and social responsibility categories. Each indicator is a dichotomous variable equal to one if the company meets the criteria established for that indicator, and zero otherwise. For example Apple, Inc. received a 1 in employee relations strengths for its supply chain labor standards, but also received a 1 for employee relations concerns for its child labor.

summing total strengths (*CSP strengths*) or total concerns (*CSP concerns*) for each of the six listed dimensions.[8]

The extant literature that discusses the validity of MSCI data finds that there are three major issues. First, it is conceptually difficult to create a rating that fully captures the complexities of positive and negative exchanges with multiple stakeholder groups (e.g., Berman et al., 1999; Chatterji et al., 2009). Second, the overall CSP score, which is commonly used in prior literature, has low explanatory power due to the netting of strengths and concerns (Mattingly and Berman, 2006). Lastly, an aggregate view of the CSP construct may be mistaken. CSP is a construct that represents a wide range of stakeholder impacts, and actions related to each of these stakeholders impact the overall construct differently and should be examined in this way (Jayachandran et al. 2013).[9] These critiques closely mirror our critique of sustainability committee measurement, and thus they are addressed in our research design.

We take guidance from Flammer (2015) when constructing our disaggregated measures of CSP. We create four sub-indices of stakeholder investment from the MSCI data, separately examining strengths and concerns related to investment in the community

[8] We also recognize that there have been critiques as to the validity of traditional constructions of CSP outcomes with MSCI data. By drawing our main conclusions and contributions from models using dimension-level MSCI data, we avoid many of the critiques of the CSP score construction process. To be sure, we perform analysis using two alternative measures of the dependent variables to ensure our results are consistent to variable specifications. We adjust all dependent variables by the industry average in each year. We also construct percentage dependent variable measurements, by dividing the scores used in the main analysis by the number of categories each firm-year was rated in. Results are consistent across all of these alternative specifications.

[9] A burgeoning literature has also addressed this issue by utilizing the split dimensions within MSCI to create tailored CSP variables (e.g., Bouslah et al., 2013; Jayachandran et al., 2013; Kabongo, Chang, and Li, 2013; Walls and Hoffman, 2013; Walls et al., 2012).[9] These studies often use individual dimensions of the KLD database, whether that be only environmental (Walls and Hoffman, 2013), only diversity (Kabongo et al. 2013), only environmental and human rights performance (Berliner and Prakash, 2014), or each of the dimensions individually (Bouslah et al., 2013). Recently, Flammer (2015) find that the impact of product market competition on CSR investment varies depending on the category of investment.

(community and human rights dimensions)[10], employees (employee relations and diversity dimensions)[11], the environment (environment dimension), and consumers and suppliers (product dimension). This method allows for both a more comprehensive analysis as well as better matching between the test and dependent variable.[12]

Independent variables

We hand-collect the information necessary for our test variable, board-level sustainability committee existence and focus. To identify these committees, we first reviewed the complete universe of unique committee names in the BoardEx database and flagged committees that are likely CSP related.[13] We took a lenient stance in our initial classification of committee names to ensure we, to the best of our abilities, identified all committees focusing on sustainability issues. Next, we manually collected the committee responsibilities as stated in the company's annual proxy filing and assessed whether they explicitly list oversight of stakeholder groups. Recognizing that committee responsibilities can fluctuate, we collect and classify data for each year of committee existence. We discovered that there are many committees that qualify as sustainability related based on their responsibility towards specific stakeholder groups, that based on key search terms in prior literature would not have been captured.[14] In contrast, we also found that many committee names suggested a sustainability related nature, but the description of their

[10] The human rights dimension deals with underprivileged groups in the community.
[11] The diversity dimension corresponds largely to actions that affect employees.
[12] While some critics of this split measure approach argue that narrow measures do not reflect the full view of a company's CSP, our study bypasses this by merely examining performance relative to the specific stakeholders focused on in the extended governance structure, rather than the broad definition of CSR.
[13] BoardEx contains data on all board committees as reported in public company proxy filings. While prior studies have used limited samples and manually searched company websites for the existence of these committees, through BoardEx we are able to identify the full scope of unique committee names.
[14] For example, unique names such as "civic & charitable affairs", "ethics, compliance, & sustainability", "employee development and retention", "excellence", "clinical quality", and more listed in Appendix A. These committees were not classified as sustainability committees by most prior studies.

responsibilities contradicted this classification.[15] In aggregate analyses for Hypotheses 1a and 1b we employ a *Committee* variable equal to one if the firm-year observation has a board-level committee with sustainability responsibilities explicitly listed in their proxy filing, and zero otherwise.

Next, we conduct a comprehensive coding of the collected committee responsibilities towards stakeholder groups. Prior to data collection, we drafted a taxonomy rooted in the MSCI dimensions of CSP, which allowed for the coding of committee responsibilities into four stakeholder groups. This taxonomy, as well as sample committee classifications, can be found in Appendix B. We create four indicator variables to represent committee foci on stakeholder groups, including *Community focus*, *Employee focus*, *Environment focus*, and *Consumer/supplier focus*.[16] For example, community committees assume responsibility for oversight of ethics compliance, charitable giving programs, housing/education programs, volunteering and community engagement, or human rights issues. Employee committees assume responsibility over internal health and safety, union relations, child labor issues, workforce diversity, and more. Environment committees, as previously examined in the literature, have responsibilities ranging from water conservation to waste management and pollution control. Lastly, consumer and supplier

[15] About 26 percent of the originally identified sample was lost due to non-CSP related descriptions. For example, committees with "employee" in their name would initially be flagged as CSP related, but upon review often had only employee stock option plan responsibilities, which we would not consider to be an element of CSP. Similarly, an "asset quality" committee was originally flagged due to its reference for quality, but was deemed unrelated as it claimed oversight for the company's credit practices and loan loss reserves. The largest portion of committees that were removed from our committee sample upon review of their responsibilities were "trust" committees, whose name may signal CSP related activity, but responsibilities consistently involved investment policies within finance industries.

[16] Two research assistants and one author independently coded committee responsibilities into focus indicator variables. The coders' initial agreement rates were above 90 percent and Cohen's kappa was over 0.80 for each category, suggesting very high intercoder agreement (Freelon 2010). The coders met to resolve their coding differences and the updated coding is used in analysis.

committees focus on product quality and safety initiatives. These focus variables are not mutually exclusive; a firm-year observation can have multiple foci if there is more than one committee for that firm-year, or if the committee focuses on multiple stakeholder groups (for example, one committee may focus on environment, employee, and consumer/supplier related issues). To properly isolate the impact of these foci, we create another set of variables for firms that have a sustainability committee that is not focused on the stakeholder group being analyzed: *No community focus, No employee focus, No environment focus, and No consumer/supplier focus*. We use these variables to draw comparisons to firms without a sustainability committee and to firms with a sustainability committee that does not focus on a specific dimension. Using our two earlier committee examples (Arch Coal and Delta Air Lines), a coding example can be found in Appendix C.

Control variables

We include several other control variables identified in prior literature as determinants of CSP (e.g., de Villiers et al., 2011; McWilliams and Siegel, 2000), including: board size, independence, tenure, board busyness, firm size, firm liquidity, firm profitability, research and development investment, and leverage. These variables are defined in Appendix A. Lastly, all models include industry and year fixed effects and standard errors clustered at the firm level.

VI. RESULTS

Descriptive statistics

Table 1.2 presents summary statistics for the variables used in our analysis. The median CSP score is zero and the mean is 0.240, suggesting that the models will largely predict a zero-baseline value of aggregate net CSP. This suggests that the net measurement of all

dimension strengths and concerns fails to capture the rich social performance data available in the MSCI dataset. Beyond splitting measurement by strengths and concerns, the separate calculation of strengths and concerns for the four dimensions of CSP also shows variation, providing evidence that each grouping represents distinct aspects of CSP. Descriptive data for control variables show similarity to those presented in recent literature (Mallin et al. 2013; de Villiers et al. 2011). On average, boards in our sample have around nine members, are 75.8 percent independent, and have a mean director tenure ranging from zero to 30 years. Sixteen percent of the boards in our sample are considered busy. Additionally, Table 1.2, Panel C presents a correlation matrix of the key variables in our analysis.[17]

[INSERT TABLE 1.2 HERE]

Figure 1.1 shows that sustainability committee are becoming increasingly prevalent throughout the sample period. It also illustrates that there is variation amongst committee foci, providing further evidence that sustainability committees are heterogeneous and should be treated as such in empirical analysis. While prior literature has focused on environmental committees (Berrone and Gomez-Mejia, 2009; Rodrigue et al., 2013), Figure 1.1 shows that consumer and supplier focused committees are the most frequently observed in our sample, followed by committees with an environment focus. Consumer and supplier committees are those that focus on the health and safety implications of product development, as well as quality, excellence, best practices, and more. We observe a steady increase in this focus throughout the sample period while other foci have remained fairly constant.

[17] For sake of presentation, only key variables (dependent variables, committee variable, and key control variables) are displayed. A full correlation matrix was examined, along with the VIF test statistic for each variable. All VIFs are below 10 in all our models suggesting that multicollinearity is not a serious problem in interpreting the results (Cohen, *et al.*, 2003).

[INSERT FIGURE 1.1 HERE]

Further, it is interesting that these committees often claim oversight of multiple stakeholder groups. It is most common for a committee to focus on two stakeholder groups at once. Figure 1.2 graphically depicts how many committees focus on multiple issues within each stakeholder focus. Further, Table 1.2, Panel D contains a complete breakdown of the various combinations of committee foci. Within community focused committees, it is common for the committee to focus on multiple issues (e.g., consumer and supplier and environment). In fact, when a committee focuses on community issues, it is common for it to focus on all of the stakeholder dimensions. When a committee focuses on environmental issues, it is uncommon for it to focus solely on that issue. Rather, this focus is often combined with a consumer and supplier focus (e.g., committees that focus on the impact of products on consumers and the environment). Combined, the varying foci of committees and the varying amount of foci in each committee motivate the use of an indicator that controls for committees that do not focus on the given outcome dimension. We are then able to compare the impact of these focus variations using coefficient comparison tests.

[INSERT FIGURE 1.2 HERE]

As this study is the first to comprehensively disaggregate the sustainability committee variable according to dimensions of CSP, these summary statistics are important to document. The heterogeneity in responsibilities evidenced by these summary statistics illustrates the need to disaggregate CSP when conducting research in this domain.

Empirical estimation results

Hypothesis 1: Aggregate performance impact of sustainability committees

In Table 1.3, we present the main findings of a sustainability committee's impact on aggregate CSP, which we discussed earlier as the motivation for our study given conflicting results in prior literature. We estimate these multivariate regressions using OLS distribution models.[18] In the first column, the sustainability committee indicator variable showed no association with net CSP (p-value of 0.204). This result is consistent with the conclusion of prior research that these committees are largely symbolic.

[INSERT TABLE 1.3 HERE]

This column illustrates the statistical reasons for research using MSCI data to split aggregate performance into strengths and concerns (Mattingly and Berman, 2006). Specifically, both test and several control variables illustrate insignificant associations with the net score, yet strong associations with both strength and concern scores.[19] Additionally, the Vuong z-statistics comparing the R^2 of the CSP score model with the CSP strengths and concerns models are highly significant, suggesting that explanatory power is much higher when CSP strengths and concerns are measured as separate constructs. Given these findings, our hypotheses and all subsequent analysis separately examine CSP strengths and concerns.

Hypothesis 1a: Sustainability committee existence and CSP strengths

[18] Given the nature of our CSP measures, we also ensure results are robust to model specifications that account for non-negative count data. Stock and Watson (2007) suggest that OLS is appropriate for count data, but that alternative specifications may better account for count data distribution. We chose to use OLS in our tabled analysis due to its ability to generate post-estimation goodness of fit measures and for easier interpretation of regression coefficients (Manner, 2010). Regressions using negative binomial and Poisson distribution specifications produce the same signs on all coefficients and similar levels of statistical significance.

[19] For an interesting example of the differential impact of a single characteristic on both CSP strengths and concerns, see Boulouta (2013). Findings of this study show that board gender diversity has a stronger influence on CSP concerns than on CSP strengths.

In Column 2, we detect a positive and significant coefficient when estimating CSP strengths (p-value = 0.000).[20] These results support H1a and provide strong empirical evidence that, within our sample, there is a significant impact of sustainability committee existence on CSP strengths. This suggests that sustainability committees view strengths as value-generating, which allows the formal commitment to stakeholders to translate into positive performance implications.

Hypothesis 1b: Sustainability committee existence and CSP concerns

In Column 3, we detect a positive and significant coefficient when estimating CSP concerns (p-value = 0.000). Given that H1b is presented in non-directional form, this finding rejects the null hypothesis in H1b.

The finding that the existence of a sustainability committee is positively associated with concerns may seem perplexing since the existence of a sustainability committee is a voluntary dedication of resources to sustainability issues. However, this finding is explained by shared value motivations where mitigating concerns does not generate value (i.e., the economic cost of mitigating concerns exceeds the cost associated with these negative impacts). In other words, a sustainability committee may exist because the board is reacting to CSP concerns that already exist or are inherent to the business.[21] Thus, it appears that the prevalence of sustainability committees is a sign that companies recognize

[20] Beyond statistical significance, it is important to discuss the economic significance of the impact detected before making practical recommendations (Bettis et al. 2016). Holding other factors constant in our sample, the existence of a sustainability committee is associated with one additional strength. Since the mean overall strengths score for the full sample is 1.83, this is a substantial 54.64 percent increase in strengths associated with the existence of a committee.

[21] We are able to identify 22 first-time committee adoptions within our sample. Univariate tests suggest that CSP concerns are significantly higher in companies that adopt a sustainability committee than in those that do not. This is consistent with a risk management explanation, where CSP concerns are risk factors that lead to the creation of a sustainability committee.

the risk negative CSP impacts pose for their business and stakeholders, but that a risk mitigation response does not follow this recognition.

Combined, H1 findings suggest that committees do not mitigate CSP concerns, but do positively impact strengths. There are various explanations for this finding. For one, committees may prioritize strengths because it easier to generate strengths than reduce concerns. Prior literature suggests that it takes longer to address concerns than it does strengths (Post et al. 2011).[22] Further, organizational change literature suggests that it is harder to enact change (i.e. reduce concerns) than it is to introduce new policies (i.e. increase strengths). Second, committees may prioritize strengths because they generate more value than concerns. Lastly, companies with sustainability committee oversight may have had even more concerns, or these concerns may have a greater negative impact, without these committees.

Hypothesis 2: Disaggregated impact of sustainability committees on CSP

Next, we further disaggregate committee existence and CSP into its stakeholder focus. We measure both sets of variables by dimension, estimating regressions pairing specific committee focus on stakeholder groups with the respective dimension of CSP, while controlling for the existence of a sustainability committee not focused on that stakeholder group. Table 1.4, Panels A and B, present results of regressions with dependent variables for paired dimension strengths and concerns, respectively.

[INSERT TABLE 1.4 HERE]

[22] Strike et al. (2006) find that R&D intensity is associated with CSP strengths, but not CSP concerns. This finding suggests that when a company invests in innovation and presumably social performance, they are able to enhance strengths, but are not able to prevent concerns.

The models include two mutually exclusive dummy variables that allow a comparison between three levels of oversight – no sustainability committee, a committee not focused on the given stakeholder group, and a committee focused on the given stakeholder group (and perhaps other stakeholders). Since H2 predicts that focused committees will be more strongly associated with paired strengths, we employ F-tests for significant differences in coefficients of focused and non-focused committees to ensure proper conclusions of differential impact.

In Panel A of Table 1.4, consistent with our predictions, we find that a committee with a community focus has a significantly greater association with community strengths than a committee not focused on the community (p-value = 0.016). These results support our method of pairing committee responsibilities with relevant CSP outcomes. The effect of a focused committee on its respective dimension of CSP is also economically significant. For instance, the community strengths model provides evidence that a committee focused on the community has 0.35 more community strengths than firms without a committee, whereas a committee not focused on the community is not significantly different those without a committee. Together, these findings suggest that the community focus matters in determining committee effectiveness. Results are consistent for environment focused committees and environmental performance. This enriches the findings of Rodrigue et al. (2013) who do not find environmental committees to have an impact on environmental performance outcomes. Also of note in these results is the effect magnitude for both employee focused and non-employee focused committees on employee related performance (coefficients of 0.80 and 0.35, respectively). These coefficients are significantly different, suggesting that employee focused committees are more strongly

associated with employee strengths than non-focused committees, but that non-focused committees are still positively associated with employee strengths. Recent literature has suggested that of all stakeholder groups, it is easiest to draw employee attention to CSR initiatives, as they are the most closely tied to the firm and may receive communications directly (Madsen and Rodgers, 2015). In our setting, it is possible that employees are more knowledgeable of their own company's governance, and are therefore are impacted by both board-level investment in their own oversight and in general stakeholder oversight.

Inconsistent with findings for the community, employee, and environment stakeholder groups, the consumer/supplier strengths model in Panel A of Table 1.4 shows no significant difference between committees that do and do not focus on the consumer/supplier dimension, with both types of committees positively impacting performance in that dimension. There are several possible explanations for this finding. First, these committees occur most frequently in our sample and their impact may be saturated. Additionally, the nature of oversight of consumers and suppliers is more closely linked to a company's financial performance (Jayachandran et al., 2013) and thus, all boards may focus on these issues, regardless of the existence of a committee focused on the issue.

When examining concerns, Panel B of Table 1.4 shows results of either a non-significant association (community and employee concerns models) or a positive association (environment and consumer/supplier models) between sustainability committee focus and relevant CSP concerns. Consistent with H1b findings, this suggests that firms with a committee are more likely to have CSP concerns than those without. Yet, except for environmental concerns, we do not find that firms with focused committees have

more concerns in the focused dimension than firms without focused committees. It largely appears that sustainability committees do not mitigate dimension concerns, regardless of committee focus. While surprising given the assumed role of corporate governance in enhancing strengths and mitigating concerns, this finding is not inconsistent with prior literature. Specifically, Walls et al. (2012), who examine a single dimension of committees and performance using the same CSP data, find that environmental committees are positively associated with both environmental strengths and concerns. Consistent with a risk management explanation, Walls et al. (2012) frame this finding as environmental committees having a dual purpose where they support environmental strengths by providing expertise and resources, and mitigate environmental concerns by placing emphasis on issues at the board level.

In sum, we find partial support for Hypothesis 2. Results suggest that community, employee, and environment focused committees are positively associated with CSP dimension strengths, which is stronger than the same association for sustainability committees not focused on these dimensions. However, we do not find that consumer/supplier focused committees have a stronger impact on consumer/supplier strengths than committees focused on other stakeholder groups. We also do not find that community, employee, or consumer/supplier focused committees have a stronger impact on CSP dimension concerns than non-focused committees.

Further characteristics impacting sustainability committee effectiveness

Thus far, our empirical analyses suggest that committee focus on community, environment, and employee stakeholder groups contributes to performance in that dimension. Yet, we acknowledge that focused sustainability committees themselves have heterogeneous

characteristics that may enhance or impede their ability to oversee stakeholder interests (Peters and Romi, 2014). To explore this, we examine three common committee characteristics that have been studied in-depth at the board-level: committee size, independence, and meeting frequency (e.g., Beeken, Stedham, and Yang, 1998; Dalton et al., 1998; Walls et al., 2012; Vafeas, 1999). Table 1.5 shows that the average sustainability committee size is around 4.5, 75.3% of sustainability committees are composed entirely of independent members and sustainability committees meet on average four times a year.[23]

[INSERT TABLE 1.5 HERE]

Next, we examine whether these characteristics contribute to the effectiveness of sustainability committees. Specifically, we stratify our committee sample into "ineffective" and "effective" committees based on their standing relative to CSP strengths[24], and examine if these additional characteristics are significantly different between ineffective and effective committees.[25] In Panel B of Table 1.5, a committee is coded "effective" if the total CSP strengths in that year is above the sample mean for firms within the specified sample (e.g., all committees, community focused committees, etc.).

Results show that committee size, independence, and meeting frequency, for the most part, positively impact the effectiveness of focused committees. These findings suggest that there is heterogeneity even within the paired committee focus and performance dimension relationship and that effectiveness of sustainability committees is greater when boards substantively dedicate resources to subcommittees operations, allowing

[23] Characteristic data is not available for all of the 1,243 committee-firm-year observations in our sample, thus the sample for this analysis is 1,196 committee-firm-year observations with complete data on committee size, independence, and meeting frequency.
[24] We choose to evaluate effectiveness based on CSP strengths, rather than net CSP or CSP concerns, given the significance and consistency of this finding in our primary analyses.
[25] We caution that a univariate analysis is used for simplicity of presentation, and that results should not be interpreted on the same level as multivariate findings for H1 and H2.

accountability to translate into performance (Dubnick 2005). This is an important practical consideration: if boards do not dedicate substantive resources to their committees, even a focused committee can fail to improve relevant performance.

CSP sensitive industry classifications

Our analysis thus far has accounted for the industry-specific nature of sustainability by including industry fixed effects in all models. However, because CSP strengths and concerns are fundamentally different across industries (Koh et al. 2014) and firm determinants of CSP may also differ across industries (Flammer, 2015), committee value considerations and effectiveness may vary across industries.[26] Therefore, just as we argue for proper pairing of committee focus and dimension of CSP (e.g., environmental committee and environmental performance), we also propose that analysis should be conducted within the proper sample of firms sensitive to that dimension of CSP (e.g., environmentally sensitive).

Prior research recognizes the industry-specific nature of CSP and performs analysis within environmentally sensitive industries (Cho et al., 2006; Rodrigue et al., 2013). We believe that this should be extended to the other three categories of stakeholders (community, employee, and consumer/supplier) and present an objective, data-driven, approach to classify industries sensitive to each dimension.[27] To execute this, we first sum

[26] For example, Denbury Resources, Inc. falls within the oil and gas extraction industry and regularly faces environmental and safety related issues. Accordingly, the company has a "Safety, Environmental, and Reserves" committee that focuses on environment and consumer/supplier related issues. Conversely, Marriott International, Inc. faces a vastly different CSP landscape as a service business within the hotels and lodging industry, and thus has an "Excellence" committee to oversee employee relations. It is evident in these examples that industry plays a large role in determining both CSP and committee focus.

[27] Despite the advantages of a quantitative approach, we do recognize that qualitative approaches have been used in prior literature and have their own advantages. These classifications consider the impact of common industry activities on a given sustainability dimension. For instance, environmentally sensitive industries are often those that are resource intensive, including oil exploration, paper, chemical and allied products, pharmaceuticals, petroleum refining, and metals (Cho et al. 2006). While common for the environment

all strengths and concerns within each dimension of MSCI data, asserting that firms with a greater sensitivity to stakeholder groups are likely to receive both more strengths and more concerns in that dimension. Next, we compute the average sum score for each dimension by industry (as grouped by 2-digit SIC code). Lastly, we classify industries as sensitive to a dimension if they are ranked within the top quartile of average sum scores.[28] This quantitative approach is unique in that it can be uniformly applied to all four sustainability dimensions as well as replicated in future large-scale research. This approach relies on the MSCI data, which is widely considered the standard for CSP research, and is replicable and generalizable to a multitude of contexts.

Table 1.6 presents the 2-digit SIC codes of industries within each of our specified sensitive samples. We perform several tests to validate our quantitative approach.[29] We further test our sensitive industry classifications by examining whether companies in sensitive industries are more likely to have a committee focused on that dimension. Firms in these industries are more likely to feel accountable to sensitive stakeholder groups than to others. Univariate comparisons presented in Table 1.6 confirm this and suggest that companies in sensitive industries are more likely to have a committee with a relevant focus

dimension, this approach is difficult to apply to all dimensions of sustainability with accuracy (e.g., for the employee dimension, all firms have employees with issues that must be managed), and to the best of our knowledge such a classification has not been done for community and consumer/supplier dimensions.

[28] Our results are robust to alternative cutoffs for the sensitive industry samples, including above the median, top quintile, and top decile.

[29] First, the resulting classification of environmentally sensitive industries encapsulates all of the resource intensive industries that have been classified as environmentally sensitive in prior literature (Cho et al. 2006). This provides comfort that our approach does not result in classifications that conflict extant qualitative research. Second, we use data external to MSCI ESG STATS to validate the employee sensitive classification. Since employee sensitive industries are likely labor intensive, we examine the mean number of employees in each two-digit industry. Industries with the most employees include general merchandise stores, food stores, hotels and other lodging places, and building materials and gardening supplies. All four of these industries are classified as employee sensitive through our quantitative process. Further, most of the industries we classify as employee sensitive are in the top quartile of number of employees. Given these validations, we feel comfortable extending our quantitative method to the two other stakeholder groups, which allows the creation of a classification that has not been done under the qualitative method.

than those not in the sensitive industry.[30] This is consistent with sustainability risk management, which we propose as an explanation for why committees appear to positively impact CSP concerns. Specifically, certain industries are more prone to impact stakeholder groups, so it appears to be common for these industries to have sustainability committees in order to ensure the risk of impact on these groups is monitored and managed to meet the company's risk appetite. Additionally, there may be greater opportunities to generate value from strengths in these industries. This test also provides independent verification for both our classification of committee responsibilities and the sensitive industry classifications.

[INSERT TABLE 1.6 HERE]

Results estimating dimension strengths and concerns within these more homogenous sensitive industry samples are presented in Table 1.7. This mimics the analysis in Table 1.4, but is restricted to the respective sensitive industry sample. In Panel A, we find that community, employee, and environment foci are all positive and significant, while a consumer/supplier focus is not significant. This provides further evidence that a committee focused on a respective dimension is positively associated with CSP strengths in that dimension and supports shared value creation, where focused committees positively influence dimension strengths because these strengths generate value. Within sensitive industries, Panel B shows that community and employee committees continue to be insignificant in estimating paired concerns. Additionally, contrary to the previous analysis,

[30] We recognize that in order to have a focused committee, the firm-year observation must be within the small portion of the sample for which a committee exists, and that this may limit the evidence provided in a full sample comparison. However, when this comparison is done within firms that have a sustainability committee, we still find a greater likelihood that firm-year observations in sensitive industries have a committee with a relevant focus. Interestingly, the consumer/supplier committee is more prevalent in industries that are not sensitive to the consumer/supplier dimension when the test is limited to those with committees. We attribute this finding to our earlier explanation that the consumer/supplier focus is the least discretionary and represents an issue that is likely considered by all firms.

consumer/supplier committees are no longer significant in estimating concerns. While a positive association remains in the environment dimension, the effect size is not greater than in the entire sample, which is unexpected given the environmental issues a sensitive industry would face. Overall, findings of concerns also support shared value creation, where focused committees determine whether dimension concerns destroy value enough to warrant mitigation.

[INSERT TABLE 1.7 HERE]

Explanatory power in these models is greater than when estimated across the full sample, suggesting that the relationship is better targeted in a more homogenous sample of firm-year observations that are sensitive to the examined dimension. In essence, to enhance committee effectiveness, it is important to align committee focus with industry needs.

VII. DISCUSSION AND CONCLUSIONS

This paper makes four major contributions. First, we present hand-collected data for a large sample of board-level sustainability committees in public companies. We find that committees are increasingly prevalent over our 2003 – 2013 sample period. Our sample demonstrates that sustainability committees are diversified and that significant variability exists within their focus. Further, these committees often have multiple foci and it is most common for a committee to focus on two stakeholder groups at once.

Second, we clarify the conflicting evidence in prior literature on the impact of a sustainability committee on aggregate CSP. Theoretically, committees appear to be motivated by shared value considerations, where stakeholder expectations are only met if they also benefit the shareholder. This is evident in committee responsibility statements and in our findings. Specifically, we find that sustainability committees are largely

successful at generating CSP strengths, but not at remediating CSP concerns. This finding is consistent with intuitive theory set forth in this paper and suggests that a sustainability committee is potentially a mechanism to improve a firm's oversight of and impact on stakeholder groups, but not at the expense of economic success.

Third, we present evidence that a disaggregated analysis should be used to examine CSP and sustainability committees. A disaggregated analysis incorporates the heterogeneous nature of the constructs we examine and recognizes that it matters which stakeholder groups a sustainability committee is accountable to. Findings illustrate that focused sustainability committees are associated with more strengths relative to firms with non-focused committees and relative to firms without a sustainability committee. For example, not only does a committee with a community focus have an impact on community performance above firms that do not have a committee, but it is also has a stronger association with community strengths than a committee not focused on the community. These findings confirm our predictions that formally claiming board-level responsibility for specific stakeholder interests results in a positive impact on performance related to these stakeholder groups. Univariate analyses illustrate that committees that do not have sufficient resources (i.e., size, independence, meeting frequency) may not be effective.

Fourth, we introduce a quantitative approach to classify CSP sensitive industries (i.e., those where dimension-specific issues are particularly salient), which can be used in future research. Results suggest that it is important for committee focus to be aligned with industry sensitivities to sustainability impacts. In our setting, this quantitative approach to industry classification has advantages over a qualitative approach (e.g., objectiveness, applicability to all dimensions of CSP, and generalizability to future research questions).

However, we do recognize that qualitative classification approaches can provide a more nuanced understanding of industry impacts and leave this open to future research.

Overall, future research should consider a similar taxonomy in constructing sustainability measures. Using the proposed method, future research can extend understanding of the heterogeneous nature of stakeholder oversight. Practically, our results provide support for public companies to consider board-level sustainability committees as a mechanism to improve firm performance. We contribute to preliminary evidence of this in prior literature by cautioning that performance impacts vary with the stakeholder focus and resource availability of the committee, as well as the industry sustainability landscape. Although the data we employ required extensive hand-collection, investors and other stakeholders interested in individual companies can manually access these same data points in a company's proxy filings. Using these more granular data should provide better insight to the performance of sustainability committees.

Part Two

Auditor Reputation Risk: Evidence of Auditor Response to Client Negative Media Coverage (co-authored with Rani Hoitash and Udi Hoitash)

I. INTRODUCTION

This study examines negative media coverage of audit clients as a factor generating auditor reputation risk.[31] Despite the importance of risk management to auditors, there is limited understanding of auditor reputation risk to date (DeFond and Zhang 2014), and it is not clear whether and how this risk is managed. To examine auditor reputation risk, we rely on a new database that quantifies negative media coverage of environmental, social, and governance (ESG) practices at a large set of public companies. We hypothesize that negative media coverage of an audit client generates auditor reputation risk and test whether and how auditors respond to this risk.

The media provides valuable insight into a company's public perception (Deephouse 2000) and can publicize firm actions that would otherwise go undetected or be considered negligible (Bednar, Boivie, and Prince 2013; Miller 2006). For example, in just a short time Chipotle has fallen from its status as an upcoming darling in the restaurant industry. The company received widespread negative media coverage (Whaba 2015) beginning with news of an E. coli outbreak and spiraling into mainstream coverage of company incidents that may otherwise have been ignored (e.g., mid-level executive charged with drug possession (Olson 2016)). This and many other recent anecdotes (e.g., British Petroleum, Volkswagen, Target, and Sony) illustrate that company reputation is often at risk due to media coverage of ESG practices.[32] When a company's reputation is at risk due to negative media attention, the reputation of various related parties may also be

[31] Reputation risk has been presented as a component of auditor business risk (i.e., the probability that auditors will suffer a loss or injury to their professional practice (Brumfield et al. 1983)) and engagement risk (Knechel et al. 2007)).

[32] Similarly, extant literature suggests companies must be environmentally conscious, socially responsible, and governmentally sound to avoid reputation loss (Bebbington, Larrinaga, and Moneva 2008).

adversely affected. In this study, we focus on the external auditor, who has incentives to monitor a client's negative media coverage and consider how it affects their own reputation risk.[33]

Research exploring the role of the media in influencing auditor behavior is very limited. In fact, to the best of our knowledge there are no archival studies in this domain, and whether or not auditors respond to client media coverage remains an unanswered question. While auditors are expected to possess independent and proprietary knowledge about their clients (Joe 2003), experimental literature suggests that media coverage of financial statement related issues may cause modification of the audit opinion. In this study, we move beyond financial statement issues to examine negative media coverage of practices unrelated to the primary audit process. It is not clear whether auditors will find coverage of such issues relevant and whether it warrants any reaction. Unlike financial statement related issues, auditors do not have influence over nor responsibility for client ESG practices, so negative coverage in this domain may have no influence on auditor behavior. However, negative media coverage could prove influential to an auditor as an important factor that elevates its own reputation risk. Specifically, negative media attention on a client's ESG activities may intensify the reputation consequences of issuing an incorrect audit opinion (e.g., potential for engagement to receive negative media attention). Further, an auditor's association with a risky client may damage its reputation even when the audit is conducted properly (Houston, Peters, and Pratt 1999). Reputation damage of this sort can lead to the loss of current and prospective clients, need to offer fee discounts

[33] Informal conversation with audit partners and staff reveal that they monitor client media coverage frequently through both formal (e.g., email alerts) and informal (e.g., increased attention when a client is covered in the news) channels.

to current clients, weakened employee recruiting efforts and damaged employee morale (Brumfield, Elliott, and Jacobson 1983; Lyon and Maher 2005; Wilson and Grimlund 1990). In this way, negative media coverage of a client can generate auditor reputation risk.

Documenting U.S. evidence of auditor reputation risk has proven difficult (DeFond and Zhang 2014). While extant literature examines reputation damage following major audit failures (e.g., Andersen) and regulator-identified audit deficiencies, a research setting must be separated from traditional audit risk considerations to properly attribute findings to reputation risk. For instance, Donelson, Ege, and Leiby (2016) examine client litigation unrelated to financial reporting, which should not impact the auditor given a lack of relation with the audit risk model. Yet, the authors still find evidence that auditor reputation is damaged when client litigation occurs and further, that auditors do not pass costs associated with this reputation damage on to the litigated client. This finding is interesting as it suggests that auditors are taking responsibility for client misconduct outside of their oversight realm.

We expand this line of research by examining auditor response to negative media coverage of client environmental, social, and governance (ESG) practices. RepRisk is a leading business intelligence provider that conducts daily screening of over 80,000 media sources (e.g., major print media, blogs, social media) for ESG risks. Generally, studies that examine media coverage select a narrow scope of major news sources in which to identify stories (e.g., Christensen 2016; Weber, Willenborg, and Zhang 2008), whereas RepRisk's coverage and automatic collection process are more extensive. The data is presented in indicator variables for 28 ESG issues, along with detail on the severity of the issue and reach of the media source (i.e., its prominence) in which the issue was identified.

Additionally, RepRisk calculates an index that captures negative media coverage of ESG practices, which is a firm-monthly combination of the aforementioned granular issue data. Since this database is new to accounting research, we conduct several validation tests to illustrate its robustness, including manually tracing RepRisk's index and granular issue data to media sources, correlating the measures with well-known reputation rankings and using a two-step Heckman correction in our main models. We conclude that this data can prove valuable for answering research questions in the accounting field and beyond.

Using this data, we follow guidance on risk response from the COSO (2004) Enterprise Risk Management framework and examine whether auditors respond to reputation risk, as captured in negative media coverage of a client's ESG practices. The COSO framework outlines four risk responses – avoid, accept, reduce, and share. If an auditor perceives that their reputation is at risk due to client negative media coverage, they can avoid the risk by resigning from the risky client, can reduce or share the risk by performing additional work or transferring a portion of the risk to the client through audit fees, or can accept the risk by continuing with the engagement with no change to audit fees. Since risk management is crucial for audit firms (Johnstone 2000; Johnstone and Bedard 2003), we predict that audit client negative media coverage will be positively associated with the likelihood of auditor change and with audit fees.

We examine these predictions within a sample of 7,754 firm-year observations from 2007-2014. Our results suggest that auditors do respond to client negative media coverage. Specifically, we find that negative media coverage of an audit client's ESG practices has a significant and positive impact on both the likelihood of auditor change and

on audit fees.[34] These findings suggest that auditors may be concerned with reputation spillover effects, and thus assess a client's media sentiment when making pricing and retention decisions. Both the auditor change and fee findings are robust. Specifically, we find that results are consistent when we use auditor resignations as the dependent variable. We further observe that a one-year change in negative media coverage is positively associated with a one-year change in audit fees. Utilizing the monthly risk data RepRisk provides, we also examine the timing of coverage peaks and find that coverage during the negotiation phase has the greatest impact on audit fees. This finding supports the risk sharing explanation, where auditors charge higher fees during negotiation (Hackenbrack, Jenkins, and Pevzner 2014) to share their reputation risk burden with their clients.

We also investigate the differential response to environmental, social, and governance categories of media coverage. We find that fees are higher when any of these risks are present, suggesting that auditors price many forms of negative media coverage. Interestingly, we find that the likelihood of auditor change is only associated with negative media coverage of governance practices. This suggests that coverage of environmental and social practices may not be egregious enough to warrant an auditor resignation. In contrast, governance practices are more salient to an auditor who must obtain an understanding of the company's organizational structure and management team during risk assessment (PCAOB 2010a).[35] This finding is consistent with media dependency theory that suggests that stakeholders gather information relevant to their decision-making from the media (Einwiller, Carroll, and Korn 2010).

[34] Firm-year observations with an auditor change are removed from the audit fee analysis.

[35] Our measure captures negative media coverage of corporate governance practices. A list of the specific practices this category can be found in Appendix 1. This measure is different from common corporate governance measures that focus on the quality of the board, such as board independence or busyness.

A unique feature of the RepRisk database is its collection from both low and high reach media sources. Prior literature is often constrained to collection of media coverage in major news outlets such as the *Wall Street Journal* or *Financial Times*. Using RepRisk data, we are able to examine auditor reputation concerns when negative media coverage of an issue escalates from a low reach (e.g., blog, social media, etc.) to a high reach (e.g., Wall Street Journal) source. We find that auditors do not respond to coverage of an issue in low reach media but do respond when the same issue moves from low to high reach media. For example, when a child labor issue is covered by a blog, an auditor would likely incorporate this information if it were important for audit risk judgments, yet we find no association with audit fees. Rather, there is only a fee response when the child labor issue escalates to a more prominent source, which suggests that the auditor reacts to protect its reputation rather than to the underlying issue. This finding is consistent with auditor response to perceived reputation risk.

We perform several supplemental analyses which illustrate that RepRisk's media-based measures of ESG practices capture auditor reputation risk beyond the risk of material misstatement and financial risk, which extant literature documents as components of auditor decision-making (e.g. Johnstone and Bedard 2001; Johnstone and Bedard 2003). First, we construct our sample in four different ways to examine if results hold when we remove firm-years with various issues. These include firms with high risk of material misstatement, which we measure in two ways: those who fail Benford's law for the normal distribution of numbers (Amiram, Bozniac, and Rouen 2015) and those with high pre-audit misstatement risk (Dechow, Ge, Larson, and Sloan 2011). We also remove firms with high financial risk, measured by negative sales growth and stock returns. Our main findings are

consistent in each of these samples. Second, we measure abnormal audit fees unexplained by risk of material misstatement and other common controls (Lobo and Zhao 2013; Dechow et al. 2011). Results are consistent when we use abnormal audit fees as the dependent variable. Third, we do not find an association between RepRisk's measures and outcomes of the risk of material misstatement (i.e., likelihood of going concern opinion, misstatement, material weakness, and level of discretionary accruals).[36] Fourth, we examine audit delay and do not find evidence that auditors increase their testing when risk arises close to the release of the audit report. This illustrates that risks associated with ESG practices identified in the media do not prompt additional testing, which supports our conclusion that these considerations are incorporated during the negotiation phase. Combined, these analyses suggest that negative media coverage measures an incremental risk that has not previously been examined, which supports our conclusion that auditor response is explained by reputation risk considerations.

Our study makes the following contributions. First, we introduce and validate a new database to the accounting literature. RepRisk quantifies negative media coverage and has several advantages over existing data sources. Importantly, information is collected from over 80,000 media outlets, allowing for a more accurate picture of overall negative media sentiment than in prior studies, which have been constrained to data in a small number of media sources. Further, the database contains coverage in media outlets that are classified as low reach, such as blogs, as well high reach, such as the *Wall Street Journal*. This feature is unique and allows an examination of media prominence and its consequences. Additionally, this data is provided on a monthly basis, creating many opportunities for

[36] This result also holds in a sample where audit fees do not increase, suggesting that these outcomes are unaffected even when auditors do not increase effort.

more accurate timing measurement. Future research can use this data in a variety of accounting and non-accounting contexts. Second, we answer recent calls for research on understanding the role of auditor reputation risk as a component of auditors' risk considerations (DeFond and Zhang 2014). This question has been difficult to address because settings to examine reputation concerns beyond those tied to the audited financial statements are not widely available. Using client negative media coverage, made available in RepRisk, allows us to address this question.

Lastly, we contribute to the auditor change and audit fee literature by presenting evidence that external auditors incorporate client media coverage into pricing and retention decisions even when it lacks relation to traditional risk considerations. This finding is also important for practice, as it documents an unanticipated economic impact of ESG events. The potential costs associated with an auditor resignation or increased audit fees provide an additional economic incentive for companies to avoid poor ESG practices. Our findings also extend an emerging accounting literature that primarily focuses on the disclosure and assurance of ESG information. We do so by examining auditor oversight of and response to ESG-related media coverage, which is an area of growing interest for practice.

The remainder of the paper is organized as follows. Section 2 reviews related literature and theory and proposes testable hypotheses. Section 3 describes the RepRisk database and our empirical methodology. Section 4 presents our results, and Section 5 is devoted to a discussion of the major findings and their implications for research and practice.

II. THEORY AND HYPOTHESES DEVELOPMENT

Auditor Reputation Risk

A limited literature examines auditor reputation risk (Asthana and Kelekar 2014; DeFond and Zhang 2014), which contributes to the probability that an auditor will suffer a loss or injury to their professional practices (Brumfield et al. 1983). Studies have examined how clients, their stakeholders, and the market responded to Andersen's diminished reputation (e.g., Asthana, Balsam, and Krishnan 2010; Barton 2005; Bewley, Chung, and McCracken 2008; Chaney and Philipich 2002). A few international studies, where litigation risk is not a confounding factor, have similarly examined the impact of an audit failure on audit firm reputation (e.g., Gao, Jamal, Liu, and Luo 2011; Skinner and Srinivasan 2012; Weber et al. 2008). Findings suggest that when there is an audit failure, an auditor's ability to provide future services is damaged. Specifically, the auditor loses clients and other clients of the auditor experience negative abnormal returns. Similar consequences are identified when audit deficiencies are identified by regulators, such as the SEC (Wilson and Grimlund 1990), AICPA peer inspectors (Hilary and Lennox 2005), and the PCAOB (Boone 2015; Dee, Lulseged, and Zhang 2011; Lennox and Pittman 2010). Further, an impaired reputation can result in the need to offer fee discounts to current clients and the loss of current and prospective clients, current and prospective employees, and a decline in employee morale (Brumfield et al. 1983; Lyon and Maher 2005; Wilson and Grimlund 1990). This body of literature illustrates that auditors have strong incentives to avoid reputation damage, but apart from consequences following the Andersen failure and regulatory action, U.S. evidence of this has yet to be documented (DeFond and Zhang 2014).

It has proven difficult to identify a setting where reputation risk can be investigated, as it is often confounded by traditional audit risk or litigation risk.[37] Further, while studies have examined reputation damage as a result of audit deficiencies and failures, examining if and how actions of affiliated parties influence auditor reputation is less common. One endeavor is by Donelson et al. (2016), who find that when an audit client is sued for reasons unrelated to financial reporting (i.e., non-GAAP securities fraud class actions), other clients in the same city-industry are awarded fee discounts. The authors conclude this reaction is consistent with an auditor's reputation being damaged and with subsequent action taken by the auditor to appease other clients, despite their independence from the damaging event. Interestingly, the authors do not find that fees are impacted for the litigated client, suggesting that auditors do not transfer this reputation damage to the client with reputation issues.

We aim to extend Donelson et al. (2016) by examining reputation spillover between an audit firm and the damaged client. To the best of our knowledge, studies have yet to identify a broad setting in which to examine auditor reputation risk. Media coverage of client practices unrelated to the primary audit process is a promising setting to fill this gap.

Negative Media Coverage

[37] Reputation risk has been presented as a component of auditor business risk (i.e., the probability that auditors will suffer a loss or injury to their professional practice (Brumfield et al. 1983)). Extant literature has focused on the litigation risk component of auditor business risk, but a recent literature review calls for evidence on reputation risk (DeFond and Zhang 2014). Documenting evidence of reputation risk has proven difficult in a U.S. setting, where litigation is often a confounding explanation (i.e., client issues that increase reputation risk also increase the likelihood that an auditor will be named in a lawsuit related to the issue, as seen in Andersen's demise). Donelson et al. (2016) begin to resolve this by examining non-GAAP related lawsuits at audit clients as an event that would not impact auditor litigation risk. For the same reason, we examine ESG issues. Untabulated results illustrate that in our sample, only seven firm-years have an auditor named in a lawsuit in connection with media coverage of an ESG issue, which suggests that our reputation risk measure does not capture litigation risk.

The media, and specifically the business press, is an important information distributor to the market. The media distributes information more broadly, regardless of whether it creates new content (Drake et al. 2014; Bushee, Core, Guay, and Hamm 2010; Huberman and Regev 2001; Miller 2006).[38] Essentially, media shapes public opinion by packaging and rebroadcasting information to a broad audience. Agenda setting theory suggests that media organizations determine what the general populations finds newsworthy and that media coverage of certain issues raises the salience of these issues in the public's agenda (Carroll and McCombs 2003; McCombs and Shaw 1972). The more attention the media gives to issues, the more likely the public will label these issues as important. This theory does not predict that the media will be successful in informing the public how they should feel about certain issues, but rather what issues they should think about. Thus, media coverage is thought to be a reasonable indicator of the public's knowledge about a firm (Deephouse 2000).

Negative media attention, in particular, has created a risky arena for managing corporate reputation.[39] In other areas of accounting research, negative media coverage has been associated with an increased cost of capital (Kothari et al. 2009), decreased stock price (Weber et al. 2008), increased stock return volatility (Kothari et al. 2009), and

[38] Miller (2006) presents evidence consistent with the dual role of the business press, where it both rebroadcasts information and conducts original investigation. Consistent with the media uncovering private information, the author finds that the press often publishes articles regarding accounting fraud prior to public acknowledgment by the firm or by the SEC.

[39] Individuals are often biased towards negative information, which is viewed as more salient and can be over-weighted in subsequent decision-making (Bednar et al. 2013). This general principle, termed negativity bias, is found across a broad range of psychological phenomena (Baumeister, Bratslavsky, Finkenauer, and Vohs 2001). Because individuals have limited cognitive resources, negative information receives more processing prominence and contributes more strongly to final impressions than positive information. Thus, it is mere human nature for the media and corporate stakeholders to focus on negative events.

increased likelihood of forced executive turnover (Farrell and Whidbee 2002).[40] This body of literature documents that negative media coverage can cause reputational and actual damage to the covered company. Given the broad dissemination of the media, negative media coverage is likely to be especially salient to certain stakeholders and can trigger change in which decision makers take action to protect reputation (Bednar et al. 2013). In this study, a company's external auditor is the stakeholder of primary interest.

Auditor Risk Assessment of Client Negative Media Coverage

Evidence of the role of negative media coverage in an audit setting is limited (Joe 2003; Mutchler, Hopwood, and McKeown 1997; Frost 1991). The referenced studies employ experimental methodology and find that media coverage of financial statement related issues (i.e., debt default or loss contingencies) is associated with modification of the audit opinion. While this finding is interesting given that auditors are expected to possess independent and proprietary knowledge about their clients (Joe 2003), it is limited in its generalizability. For one, archival evidence of auditor response to media coverage has not been documented. Additionally, it is unclear whether auditors consider coverage of issues unrelated to the audit process to be important. These unrelated issues, such as child labor or local pollution, lie outside of the primary audit process and thus, an auditor's realm of consideration. However, coverage of unrelated issues may prove valuable to an auditors' risk assessment of current clients in a unique way. Specifically, audit client negative media coverage may escalate into auditor reputation risk.

[40] Further, two recent working papers suggest that negative media attention influences change at the covered company. Chen, Powers, and Stomberg (2015) find that firms react to negative media attention about their tax practices by decreasing income tax footnote disclosure readability, but not their actual tax avoidance. Conversely, Dhaliwal, Goodman, Hoffman, and Schwab (2016) find that firms with negative media scrutiny during the Occupy Wall Street window exhibit lower levels of tax avoidance in the following periods.

Although auditor reputation risk is not formally expressed in the components of the audit risk model (PCAOB 2010a), an auditor may set audit risk more stringently when there are greater perceived consequences of an incorrect opinion. This can occur when a client is already under media scrutiny, and an auditor believes that its engagement may also receive media attention. Additionally, when a client is subject to negative media coverage, an auditor's reputation may decline merely because of an association with that client, even if the auditor fully complies with auditing standards (Houston et al. 1999). While the auditor is most likely not responsible for the actions that lead to the negative media coverage, it may nonetheless affect its own reputation. That is, the auditor may be perceived guilty by association, which will impact its overall reputation risk.

If auditors perceive there to be risks of reputation spillover, they are motivated to digest news about their clients' practices to avoid losses to their own business. In this way, client practices that the media is bringing to the public's attention that may not otherwise impact traditional engagement risk considerations are incorporated into auditor risk assessment.

Auditor Risk Response to Client Negative Media Coverage

Given the logic presented above, an audit firm is motivated to monitor media criticism of their clients and consider whether their firm could face increased reputation risk as a result. We now turn to predicting how auditors respond when this risk is perceived. Auditors face a risk and return trade-off decision when managing client relationships (Johnstone and Bedard 2003). Risk management is crucial for audit firms, who seek to balance the possibility of business losses (e.g., loss of clients, employees, need to offer fee discounts, etc.) stemming from increased auditor reputation risk with the desire for client revenue.

If client negative media coverage increases auditor reputation risk, audit firms will presumably take action to compensate for reputation-related losses and to avoid future reputation damage. The COSO (2004) ERM framework provides a useful guide to examine the potential response to this risk.[41] In the risk response phase of COSO (2004), an entity seeks appropriate action to align risk with associated tolerances and appetite. These responses include: avoid, accept, reduce, and share. The chosen risk response must be realistic, taking into account costs and benefits of responding to the associated risk (i.e., the reasonableness of response choice and severity given additional risk burden). In a review of auditor response to litigation risk, DeFond and Zhang (2014) identify the following responses: (a) reducing or bearing risk by adjusting audit fees and (b) avoiding risk through client retention and acceptance. We hypothesize that these are also the primary options in responding to increased reputation risk.

Risk Response: Avoidance

An avoidance response entails exiting the activity giving rise to risk (COSO 2004). Audit firms can avoid future reputation risk by departing from a controversial client. Recently, the literature has shown that auditors consider multiple risk factors – audit risk, business risk, and auditor litigation risk – in resignation decisions (Ghosh and Yang 2015). The avoidance response suggests that no response can be identified that can reduce risk consequences to an acceptable level (COSO 2004). When a client creates an unacceptable

[41] This framework is a detailed guide by which companies can approach risk management. In an omission that has been noted by many scholars (e.g., Eccles, Newquist, and Schatz 2007), reputation risk is surprisingly absent from the framework. While the framework is designed for client's to assess their own business risks, it is also helpful for the auditor to incorporate this understanding of business risk into their own risk assessment process.

level of risk for the audit firm, auditors may choose to resign to avoid negative consequences. We predict this in our first hypothesis.

> **Hypothesis 1:** The likelihood of an auditor change is positively associated with client negative media coverage.

Risk Response: Reduce or Share

A reduction or sharing response reduces risk to an acceptable level by transferring a portion of the risk (COSO 2004). If an audit firm does not deem risk to be egregious enough to warrant resignation, they may reduce risk by transferring it to the client through pricing decisions. Under the Simunic (1980) audit fee model, audit fees could increase for at least two reasons. First, risk may impact the production component of the audit fee model. If the potential for reputation risk spillover exists and an auditor limits the acceptable level of audit risk, the auditor may increase effort in response. Second, risk may impact the expected loss component of the model, where reputation risk increases the expected future losses from reputation losses. An auditor can still face reputation damage even when in full compliance with auditing standards, so increased effort does not eliminate reputation risk (DeFond and Zhang (2014). In this case, the auditor may charge the client a fee premium as compensation for the additional reputation risk. The auditor has incentives to be aggressive with risky clients to minimize potential reputation loss. Presumably, risky clients are not in a position to resist a fee increase as this sort of disagreement could lead to auditor resignation, which would create further risk and associated costs. Thus, audit clients with greater negative media coverage may bear the expected costs of reputation risk in the form of higher audit fees, which reflects effort, a risk premium, or both.

Recent literature has found support for the pricing of client misconduct, as evidenced by a positive association between a misconduct incident and audit fees

(Donohue and Knechel 2014; Lyon and Maher 2005; Ye, Simunic, and Li 2016).[42] We expect consistent reactions to our broad media-based measures and predict this in our second hypothesis.

Hypothesis 2: Audit fees are positively associated with client negative media coverage.

III. RESEARCH DESIGN

Sample

Our sample consists of 7,754 firm-years covered in the RepRisk database from 2007-2014[43] and with complete dependent and control variable data in Compustat and Audit Analytics. Information on the derivation of our final sample can be found in Table 2.1.

[INSERT TABLE 2.1 HERE]

Measuring Clients' Negative Media Coverage

Our study relies on the RepRisk database to measure client negative media coverage. This unique database contains various measures of negative media coverage of environmental, social, and governance issues of companies.[44] Whereas previous media literature limits search to selected major news sources to identify articles that are most salient to the public, this database allows for an aggregation of over 80,000 media sources into a composite metric. Since collection is broad, RepRisk likely provides a more accurate measure of

[42] Lyon and Maher (2005) present international evidence of a significant association between alleged client misconduct, as measured by the payment of bribes to high-level foreign government officials, and audit fees. They encourage future research to examine other types of misconduct unrelated to auditors' primary responsibilities to see whether this association holds.

[43] RepRisk coverage begins in 2007.

[44] In a different context, Christensen (2016) employs a similar construct. The author defines "CSR-related misconduct" as events related to social and environmental issues, which overlap with many of the granular issues RepRisk collects. The author collects these incidents solely from their coverage in reputable international business news sources (e.g., Wall Street Journal, Financial Times, etc.). Findings illustrate that corporate accountability reports can insulate a company's stock price decline following CSR-related misconduct.

overall negative media sentiment that cannot be observed by collecting data from a single news outlet. To the best of our knowledge, our study is the first to use this database in the accounting literature.[45]

RepRisk originated as a credit risk department at UBS, a global bank in Switzerland. In response to a request by UBS, in 2006 RepRisk developed a proprietary framework to identify and assess company exposure to ESG risks. Since development, RepRisk data has been used as a metric for inclusion in the Dow Jones Sustainability Indices, as a component of Newsweek's Green Rankings, and as a partner to the Carbon Disclosure Project and the Sustainability Accounting Standards Board to support the annual review of companies' risks and develop related standards and guidelines. RepRisk has a variety of clients such as banks, asset managers, insurance companies, and corporations; in fact, a recent survey of analysts at a major European bank cites RepRisk as the primary source of corporate social performance information (Luo, Wang, Raithel, and Zheng 2015). RepRisk has also proven to be an externally valid measure of negative media coverage. Volkswagen is an interesting anecdote. According to internal documents, RepRisk was the only ESG research provider to flag the ESG issues related to Volkswagen ahead of the September 2015 emission scandal (RepRisk 2015). At a granular issue level, they had published issues related to incorrect emission and fuel consumption statements in 2013. Confirming the comprehensive nature of collection processes, they also identified

[45] In fact, the use of RepRisk in other literatures is also very limited. To the best of our knowledge, a recent study by Kolbel et al. (2017) was the first to introduce this database to academic research. In their study, the index of negative media coverage is employed as a measure of media-based public pressure to examine how it impacts other elements of firm risk. We extend this logic to the auditor, a known related party to the client being criticized.

the 2015 scandal a day before it broke in mainstream media due to a story from a German NGO.

To construct the database, RepRisk uses artificial intelligence to conduct searches for negative coverage across 28 ESG issues. These issues are listed in Appendix D. Third party sources in fifteen languages are examined (e.g. major print media, thousands of NGOs, newsletters, news sites, governmental agencies, blogs, and social media).[46] RepRisk focuses on selectively collecting criticism or negative news on companies, which avoids potential window-dressing (i.e. boasting of positive ESG actions to mask issues) done in company issued reports. The 28 issues selected by RepRisk represent major categories within a company's environmental, social, and governance activity.[47] All principles of the United Nations Global Compact are captured in these issues, providing further validity to its scope. After source data is collected, trained analysts then examine and verify the data before linking it to the 28 issue categories.

Issue data is compiled into an index that captures negative media coverage of ESG practices. This compilation occurs using a proprietary algorithm, which calculates the index based on the identified issues, the severity of the issues, the reach of media sources, and the frequency and timing of information. The severity of the issue is a function of the consequences of the issue (e.g., no further consequences, injury, death), the extent of the issue (one person, a group of people, a large number of people), and the cause of the issue (negligence, intent, systematic). The reach of the media source is a pre-classified

[46] RepRisk constructs its universe of companies with a data-driven approach. Specifically, the granular issues are comprehensively collected using artificial intelligence, and a company is included in the sample to the extent they have had an ESG issue over the period 2007-2015.

[47] These issues encompass individual reputation risk factors that have been examined in prior literature. For instance, the illegal bribery that Lyon and Maher (2005) examine would be captured by this issue search in the governance category: "corruption, bribery, extortion, money laundering."

determination, where international media (e.g., Financial Times, New York Times, BBC, etc.) is weighted higher in the index than low influence sources such as local media, blogs, and internet sites.[48] Further, the frequency and timing of the issue is important because news is only entered into the database to impact the index once, unless escalated to a more influential source (e.g. a Wall Street Journal article results in a larger index increase than a blog entry), appears again after six weeks, or additional issues related to the story emerge.

Test Variables

Our primary test variables include (a) a continuous index measure of negative media coverage of client ESG practices (*NEG_MEDIA)*, and (b) granular measures of the existence of environmental, social, and governance coverage (*E_ISSUE*, *S_ISSUE*, and *G_ISSUE*). Given the availability of monthly data in RepRisk, we are uniquely able to match the timing of our test and dependent variables. To match the RepRisk data with firm-specific information in Compustat and Audit Analytics, we transform the monthly data for these data points by taking the maximum index within a specific period.[49] For the primary analyses, the index is taken within the audit negotiation period, when an audit firm makes client retention and fee contract decisions (Hackenbrack et al. 2014).[50] This negotiation

[48] We manually verify well-known ESG incidents within this granular data. Specifically, we traced coverage moving from low to high severity and low to high reach and it's consistent with descriptions of the variables provided by RepRisk. For example, in November of 2009 Apple Inc. experienced negative media coverage of their use of child labor, damaging their reputation. RepRisk data shows the index jumping from 24 to 39 in November of 2009, when multiple issues of high severity were identified in the following categories: supply chain, poor employment conditions, occupational health and safety, human rights, and child abuse. These issues had been previously identified in less influential media sources, but the index was further increased as negative media coverage escalated.

[49] We use the maximum index because the auditor is likely to react to peak risk, rather than average risk. Results are consistent if the average over the negotiation period is taken.

[50] Hackenbrack et al. (2014) interview Big 4 partners to develop a timeline for auditor-client negotiations. Findings show that the engagement letter is a fixed fee contract and that subsequent billing in addition to the negotiated audit fee is rare. Because it is difficult to alter the negotiated fee, auditors spend time considering new developments in standards, client operations, client industry, and the economy before engagement letter signing.

concludes with engagement letter signing during the first quarter of the fiscal year under audit; thus, to capture risk most salient to the negotiation, negative media coverage is measured within the six months that span the fourth quarter of *t-1* and the first quarter of *t*. Figure 2.1, which is adapted from Hackenbrack et al. (2014), provides further information on the timing of risk measurement. Our primary measure of negative media coverage is *NEG_MEDIA*, which is measured as the index during the negotiation period, adjusted by the mean index for all companies in the sample measured during the negotiation period.[51]

[INSERT FIGURE 2.1 HERE]

RepRisk provides rich issue data, which we also examine in our study. We create three indicator variables for the coverage of an issue in each of the following categories: environment, social and governance, *E_ISSUE, S_ ISSUE,* and *G_ ISSUE,* respectively. These variables are equal to one if a firm year has a granular issue within the respective broad category, and zero otherwise. Environmental issues surround those related to a company's environmental footprint and include pollution, overuse of resources, waste issues, animal mistreatment, etc. Social issues surround community and employee relations and include human rights and discrimination as well as labor issues. Lastly, governance issues range from corruption to executive compensation, anti-competitive practices, and fraud.

Measuring Auditor Response

Auditor Change and Resignations

To test H1, we regress *NEG_MEDIA* on the likelihood of auditor change. *AUDITORCHANGE* is an indicator variable equal to one if a firm-year observation has an

[51] This adjustment is made to address the expansion of RepRisk operations and ability to measure reputation risk over our sample period, which resulted in more risks identified over time.

auditor change in the current year. We also examine the impact of *NEG_MEDIA* on *RESIGN*, which is an indicator variable equal to one if a firm-year observation has an auditor resignation in the current year. H1 predicts that β_1 will be positive and significant in both models. We also present separate models that replace *NEG_MEDIA* with *E_ ISSUE, S_ ISSUE,* and *G_ISSUE*, and expect each of these issue indicators to be positive and significant.

$$AUDITORCHANGE/RESIGN = \beta_0 + \beta_1 NEG\_MEDIA + \beta_2 LNASSETS + \beta_3 ROA + \beta_4 LEVERAGE + \beta_5 SALESGROWTH + \beta_6 BANKRUPTCY + \beta_7 MA + \beta_8 FOREIGN + \beta_9 P\_SCORE + \beta_{10} RESTATEMENT + \beta_{11} GC + \beta_{12} LOGAUDITFEES + \beta_{13} INDUSTRYEXP + YEAR\ AND\ INDUSTRY\ FIXED\ EFFECTS + \varepsilon \quad (1)$$

Our empirical models control for other known factors that affect auditor changes (e.g., Stefaniak, Robertson, and Houston 2009; Mande and Son 2013). We expect auditor changes to occur more frequently when: firms are larger (*LNASSETS),* less profitable (*ROA)*, riskier (*LEVERAGE, SALESGROWTH, ZSCORE),* have merger and acquisition events *(MA)*, and have foreign operations (*FOREIGN*). We also expect auditor changes to occur more frequently when clients have a higher risk of material misstatement (*P_SCORE*), when the auditor discloses a restatement or going concern *(RESTATEMENT, GC),* when audit fees are low (*LOGAUDITFEES)* and when the auditor is not an industry expert (*INDUSTRYEXP).* The models also control for year and industry (two-digit SIC code) fixed effects and standard errors are clustered by firm.

Audit Fees

To test H2, we regress the negative media coverage measures on the natural logarithm of audit fees (*LOGAUDITFEES)*. According to predictions in H2, we expect β_1 to be positive when estimating the total audit fees paid. Consistent with the auditor change model

presented, we present three additional models that replace *NEG_MEDIA* with *E_ISSUE, S_ISSUE*, and *G_ISSUE*.

$$LOGAUDITFEES = \beta_0 + \beta_1\, NEG\_MEDIA + \beta_2 LNASSETS + \beta_3 LEVERAGE + \beta_4 SALESGROWTH + \beta_5 BANKRUPTCY + \beta_6 MA + \beta_7 FOREIGN + \beta_8 FYE\_DEC + \beta_9 SEGMENTS + \beta_{10} P\_SCORE + \beta_{11} RESTATEMENT + \beta_{12} GC + \beta_{13} MW + \beta_{14} INDUSTRYEXP + YEAR\ AND\ INDUSTRY\ FIXED\ EFFECTS + \varepsilon \quad (2)$$

We remove any firm that had an auditor change from this sample to adequately test our prediction that if the auditor does not avoid reputation risk, they share the risk burden through fees. Following a recent literature synthesis by DeFond and Zhang (2014), we include a variety of known factors that impact audit fees. All variable measurements are defined in Appendix E. We expect higher fees among larger (*LNASSETS*), riskier (*LEVERAGE, ZSCORE, P_SCORE, RESTATEMENT, MW),* lower performing (*SALESGROWTH*, *ROA, GC),* more complex (*MA*, *FOREIGN, SEGMENTS)*, when the auditor is an industry expert (*INDUSTRYEXP*), and for firms with year-end that is during the auditor's busy season *(FYE_DEC)*.[52] The models also control for year and industry fixed effects and standard errors are clustered by firm.

IV. RESULTS

Descriptive Statistics

Table 2.2 displays summary statistics of test, dependent, and control variables (Panel A) and a correlation matrix of these variables (Panel B). The raw values of RepRisk's index within our sample have a median of 0 and a mean of 10.171. The median of 0 represents companies who have had negative media coverage in the past, but not in the current

[52] Due to a high correlation between auditor size and industry expertise (*INDUSTRYEXP*), we do not control for auditor size in the tabled results. However, results are consistent when *INDUSTRYEXP* is substituted with a Big 6 indicator.

negotiation period. According to RepRisk, the mean value falls within the low media exposure bucket. In fact, the large majority of observations have low media exposure, making any variation in this measure meaningful. Given a rising trend in raw index values throughout the sample period, we employ *a NEG_MEDIA* measure adjusted by negotiation period mean in all analyses. Summary statistics of indicators for environmental, social, and governance issues are also displayed. 12.6 percent of firm-year observations in our sample have environmental issues, 16.0 percent have social issues, and 10.7 percent have governance issues.

[INSERT TABLE 2.2 HERE]

To validate that negative media coverage is associated with audit client reputation damage that could spill over to the auditor, we examine its correlation with two popular reputation rankings. Fortune magazine produces a Most Admired companies list and Newsweek produces a Green rankings list. These rankings consider both positive and negative aspects of reputation. As we expect, our primary measure of client negative media coverage (*NEG_MEDIA*) is negatively correlated with these rankings.

Table 2.2, Panel A also presents descriptive statistics for the for dependent and control variables. Audit fees are, on average, $3,837,775, and 2.9 percent of observations within our sample have an auditor switch during the year. Other firm characteristics are disclosed and are consistent with prior literature.

Table 2.3 displays industry distribution within our sample, as well as *NEG_MEDIA* values and frequency of granular ESG issues within these industries. For the sake of presentation, we use the Fama-French 12 industry classification. While the industry distribution is fairly even, a few industries stand out, including manufacturing, business

equipment, wholesale, and other. However, these are not the industries with the highest *NEG_MEDIA*, which provides comfort that our sample is not purely weighted towards those receiving the highest negative media coverage. Industries with the highest *NEG_MEDIA* values include consumer nondurable goods, chemical and allied products, and utilities. The industry breakdown of ESG issues is also interesting and may encourage future research.

[INSERT TABLE 2.3 HERE]

Multivariate Results

Auditor Change: Results of Testing H1

Table 2.4 presents the results of estimating equation (1), which examines the association of client negative media coverage and the likelihood of an auditor change occurring. Each column represents a different measure of client negative media coverage. Column (1) suggests that overall coverage of ESG practices, as measured by *NEG_MEDIA*, is positively associated with the likelihood of an auditor change occurring. This finding supports H1. This result is also economically significant. We calculate the economic significance as the change in the likelihood of auditor change when *NEG_MEDIA* moves from the 25th percentile to the 75th percentile. Holding all factors at their sample mean, we observe a 10.52 percent increase in auditor change likelihood.

[INSERT TABLE 2.4 HERE]

We also examine whether auditor changes are more likely in response to all types of media coverage compiled into *NEG_MEDIA*. Interestingly, we do not find a significant response to coverage of environmental and social issues, but do find a significant effect for coverage of governance issues. Here, we calculate economic significance as the change in

the likelihood of auditor change when *G_ISSUE* moves from zero to one. A firm with coverage of a governance issue is associated with a 40.88 percent increase in the likelihood of auditor change when all other variables are measured at their sample mean.[53] Combined, these granular results suggest that an auditor is more likely to respond to coverage of governance issues and that these issues are driving the positive association with the index measurement. These results suggest that coverage of governance issues is most likely to generate auditor reputation risk, which is not surprising considering the auditor's proximity to client governance.

Our theory is particularly focused on resignations, as we argue that the auditor initiates the change to avoid reputation risk spillover. However, an auditor change is not often classified as a resignation or dismissal because disclosure of reasoning beyond accounting disagreements is voluntary and infrequent (Hackenbrack and Hogan 2002). For this reason, we employ an auditor change variable in Table 2.4 that captures both resignations and dismissals and conduct sensitivity analyses to ensure our interpretation that auditors depart from controversial clients when an unacceptable level of risk is created is valid. Specifically, we replace the dependent variable of our H1 analysis with *RESIGN.* Table 2.5 presents results of this analysis.[54] Results show that client negative media coverage is positively associated with the likelihood of resignation and that the likelihood of resignation increases by 19.50 percent as *NEG_MEDIA* moves from the 25th to 75th

[53] It is important to note that the economic significance in models with an indicator variable capturing a low frequency event (e.g., auditor changes or resignations) will be relatively high. This is primarily because our calculation holds all other variables at their sample mean, when they would likely be changing at the same time.

[54]The sample size reported in Table 2.5 is smaller than in Table 2.4. This is expected, as the number of observations differs across logit models because observations with perfect prediction of success or failure are dropped from analysis. For example, in Model (1) 203 observations with a two-digit SIC code of 37 are dropped because there are no observations in the transportation equipment industry that have an auditor resignation (i.e., the industry fixed effect perfectly predicts failure).

percentile. Consistent with our H1 findings, auditors appear to resign in response to coverage of governance issues only. Notwithstanding the unreliable nature of the classification into resignations and dismissals, this finding supports our interpretation that auditors initiate the change when risks become too egregious to accept.

[INSERT TABLE 2.5 HERE]

Audit Fees: Results of Testing H2

Table 2.6, Panel A presents the results of estimating equation (2), which examines the association of client negative media coverage and audit fees. Results in Column 1 suggest that client negative media coverage, as measured by *NEG_MEDIA*, is positively associated with audit fees. This result is also economically significant. Holding other variables at their sample mean, when *NEG_MEDIA* moves from the 25th percentile to the 75th percentile, we find a 4.79 percent increase in audit fees, which is a substantial and equals $101,584 for an average firm. We further investigate the strength of these findings in Panels B and C of Table 2.6. Panel B presents a model which shows the one-year change in *NEG_MEDIA* is also positively associated with a one-year change in audit fees. This provides stronger evidence that the positive association with audit fees is in response to increased negative media coverage.[55]

[INSERT TABLE 2.6 HERE]

[55] In untabulated analyses, we also test for an association between *NEG_MEDIA* and the auditor response variables before coverage became high-profile. Specifically, we isolate our sample to firms that are not in the top decile of *NEG_MEDIA* in the current year but are in the following year. If our response variables are driven by inherent characteristics of these companies, we would detect an association with the likelihood of auditor change and audit fees even in the year before coverage becomes high-profile (i.e., when *NEG_MEDIA* is low). In contrast, if auditor response is in fact due to increased negative media coverage as our results suggest, then we should not find an association at this time. Consistent with the latter, we find no association between *NEG_MEDIA* and auditor changes or fees within this isolated sample (i.e., during the period where negative media is low). This null result provides further support for the conclusion that *NEG_MEDIA* is driving auditor response and not a confounding variable.

In Table 2.6, Panel A we also find that audit fees are positively associated with all three issue categories, suggesting that audit fees reflect coverage of environmental, social, and governance issues. This is in contrast to our findings for H1, where auditor changes appear to be primarily driven by coverage of governance issues. Combined, these results are interesting and suggest that auditors will choose a more severe reaction, such as resignation, only for firms with governance-driven coverage. In contrast, our evidence shows that increasing audit fees is the more common response to coverage of environmental and social issues. We perform coefficient comparison tests to determine whether coverage of governance issues is priced more than coverage of environmental and social issues. We find that coverage of governance issues has a greater impact on audit fees than coverage of social issues ($p<0.10$), but is not significantly different from coverage of environmental issues ($p>0.10$). Coverage of environmental and social issues are also not significantly different ($p>0.10$).

Overall these results support H2. The finding that client negative media coverage is positively associated with audit fees suggests that audit fees reflect increased effort, a risk premium, or both. Further, this evidence that auditors are successfully able to increase fees may indicate that auditors have greater negotiating power over clients with reputation pressures. These clients likely wish to avoid disagreements with their auditor that could lead to further negative media coverage and reputation consequences, and therefore may be more likely to agree to share risk with their auditor.

To explore this explanation, Panel C presents an analysis that examines the timing of the peak in a client's negative media coverage during different periods of the audit process to determine whether an auditor reacts in periods where negotiation is likely to

occur. Figure 2.1 depicts the timing of each variable's measurement. To execute this analysis, we isolate *NEG_MEDIA* that peaks in certain periods while remaining low in others. Specifically, we remove the middle quintile of *NEG_MEDIA* and measure peak coverage as the top two quintiles and low risk as the bottom two quintiles.

In Column (1), we examine coverage that peaks in the previous period but is low in the negotiation and subsequent period. To capture this, *NEGMEDIA_PEAK_PRIOR* is an indicator variable equal to one if *NEG_MEDIA* within the first through third quarters of *t*-1 is in the top two quintiles and if *NEG_MEDIA* in the fourth quarter of *t*-1 and throughout year *t* is in the bottom two quintiles. This effectively compares coverage that peaks in prior periods versus coverage that remains low throughout. The null finding in this column illustrates that negative coverage in previous periods is not associated with auditors' response in the current period (i.e., audit fees in period *t*). One interpretation of this finding is that auditors do not increase audit fees (via effort) based on risks identified in the prior audit, which is not surprising given the stickiness of audit fees.

In Column (2), we examine coverage that peaks in the negotiation period but is negligible within the subsequent period. With this sort of coverage peak, we predict that an auditor will adjust their fees due to reputation concerns in advance of the audit's conduct. *NEGMEDIA_PEAK_NEGOT* is an indicator variable equal to one if *NEG_MEDIA* within the negotiation period (i.e., the fourth quarter of *t*-1 and the first quarter of *t*) is in the top two quintiles and if *NEG_MEDIA* in the subsequent period (i.e. the second through fourth quarters of *t*) is in the bottom two quintiles. The positive association detected between *NEGMEDIA_PEAK_NEGOT* and *LOGAUDITFEES* suggests that negative coverage that peaks in the negotiation period is more strongly

incorporated into pricing than risk that is low throughout. An auditor appears to incorporate risk into the fixed fee contract rather than subsequently billing the client for the risk in later periods (Hackenbrack et al. 2014).

Lastly, in Column (3), we test the opposite of Column (2), where coverage peaks in the subsequent period but is negligible during the negotiation period. *NEGMEDIA_PEAK_SUBSEQ* is an indicator variable equal to one if *NEG_MEDIA* within the period subsequent to the negotiation period is in the top two quintiles and if *NEG_MEDIA* in the negotiation period is in the bottom two quintiles. Results show a significant and positive association between *NEGMEDIA_PEAK_SUBSEQ* and *LOGAUDITFEES*, which suggests that when negative coverage appears during the audit, procedures are in fact adjusted as expected in a risk of material misstatement explanation. However, we observe that the magnitude of the coefficient in Column (2) is more than double the magnitude of the coefficient in Column (3), which suggest that the economic effect is more salient when coverage peaks during the negotiation period. Overall this analysis suggests that auditor response is stronger in the negotiation period when the fee premium is set than in the subsequent period when effort is altered. This is consistent with the risk sharing response under COSO.

Supplemental Analyses

Reaction to Level of Media Sources

Table 2.7 presents results examining audit fee response when identified issues move from low reach media sources (e.g., social media, blogs, etc.) to high reach media sources (e.g., The Wall Street Journal, Financial Times, etc.). Regardless of how publicized issues are, an auditor is expected to incorporate any risk that could result in material misstatement in

their audit plan. Thus, if our measures are reflective of the risk of material misstatement, we would expect a response regardless of the reach of media source and would not expect a significant response when publicity increases. However, if our measure is reflective of reputation risk, we would expect a significant response when an issue moves from a low reach media source to a high reach media source.[56] This movement increases visibility on a risky client and its auditor. *LOWHIGH_SUM* is a count variable of individual issues (as displayed in Appendix D) that move from a low reach media source in *t*-1 to a high reach media source in *t*. In Column (1) we measure these variables in time *t*+1 to examine whether fees are impacted in the year prior to when coverage of the issue moves from low to high reach. We do not detect a significant association between *LOWHIGH_SUM_LEAD* and *LOGAUDITFEES*. It does not appear that auditors react to coverage in low reach media sources in the year before the coverage is elevated to high reach sources. This again suggests that results are reflective of reputation risk and not the risk of material misstatement; if so, an auditor would have increased effort regardless of the media outlet. Conversely, in Column (2) we find a significant and positive association between *LOWHIGH_SUM* and *LOGAUDITFEES*, which suggests that pricing is impacted when an issue is elevated from a low to high reach media source. Given the media's influence on public opinion, this is consistent with auditors reacting to protect their reputation in response to a client's high-profile negative media coverage.

[INSERT TABLE 2.7 HERE]

[56] For example, Safeway, Inc. had highly publicized ESG issues (product-related health and environmental issues, supply chain, and corruption) in 2010. These issues were identified in low reach media sources (e.g., blogs, internet sites) earlier, in 2009. Because auditors continuously monitor client risk factors, they presumably had knowledge of these issues even when they were reported in low reach media in 2009. The analysis in Table 7 examines auditor response when issues, such as this example, are in low reach media sources, and when they move from low to high reach media sources.

Investigating Alternative Explanations

In addition to the explanation that auditors react to protect their reputation by resigning from risky clients and charging a fee premium to clients they retain, we must also explore whether the positive association between client negative media coverage and audit fees is reflective of the auditors' increased effort. Specifically, if the media reveal private information on inherent or control risk factors that an auditor has no previous knowledge of, an auditor's judgment of the risk of material misstatement may increase. When this occurs, the audit risk model illustrates that an auditor should alter the nature, extent, and timing of procedures to maintain the target level of total audit risk (PCAOB 2010b). We conduct multiple supplemental analyses to ensure that our audit fee results are not driven by this increased effort explanation, which would be inconsistent with reputation motivated responses.

Sample Isolations

Table 2.8 presents results estimating our main hypotheses in samples where firm-years with various risk issues are removed. Our results could be confounded if *NEG_MEDIA* is associated with the risk of material misstatement or financial risk. The first two columns of each panel remove firms with high risk of material misstatement. In the first column, firms who fail Benford's law are removed.[57] Amiram et al. (2015) demonstrate that disagreement with Benford's law can be used as a proxy for the level of error in financial statements. In the second column, firms with high pre-audit misstatement risk (Lobo and Zhao 2013; estimated using the Dechow et al. (2011) predicted probability of

[57] Benford's law states that in random samples, the leading digits of all numeric values will conform to the Benford distribution, where increasing numbers appear with decreasing frequency (Hill 1995; Amiram et al. 2015).

misstatement) are removed. Columns 3 and 4 of each panel remove firms with high levels of financial risk, which could materialize in audit risk. In the third column, firms with decreased sales are removed. In the fourth column, firms with negative stock returns are moved.

[INSERT TABLE 2.8 HERE]

In both Panels A and B of Table 2.8, we find that results are consistent regardless of the sample isolation. Even when firms perform well (in terms of financial reporting quality and accounting/market performance), auditors still appear to react to client negative media coverage. This suggests that *NEG_MEDIA* captures risk incremental to those that are typically monitored by the external auditor.

Abnormal Audit Fee Measure

To examine the robustness of our finding that auditors price client negative media coverage, we use the Lobo and Zhao (2013) abnormal audit fee measure as our dependent variable, which measures fees beyond the expected level under normal circumstances. *ABFEE* is defined as the difference between the actual and fitted values of audit fees estimated as a function of misstatement risk and other control variables (Lobo and Zhao 2013). Table 2.9 presents results re-estimating Model (2) with *ABFEE* as the dependent variable. Results are consistent, which suggests that fees are capturing risks not expected from client characteristics and risk factors.

[INSERT TABLE 2.9 HERE]

Impact on Business Risk and Financial Reporting Failures

We also examine whether client negative media coverage of ESG practices results in risk of material misstatement that materializes, as evidenced by the effect of *NEG_MEDIA* on

traditional business risk and financial reporting quality measures. An increase in the risk of material misstatement without change to audit procedures is likely to lead to misstatements in those periods; we, therefore, examine the association between *NEG_MEDIA* and the likelihood of misstatement. We also examine three other commonly examined outcomes of the audit process: the likelihood of going concern, material weakness, and the amount of discretionary accruals. Table 2.10, Panel A presents findings within our full sample. Results illustrate that *NEG_MEDIA* is not significantly associated with any of these outcomes. These findings suggest that our media-based measure does not impact the risk of material misstatement, or that auditors respond to an increased risk of material misstatement by altering procedures to prevent poor financial reporting quality.

[INSERT TABLE 2.10 HERE]

To examine the latter explanation, we conduct further analysis. Specifically, it is possible that client negative media coverage is reflective of the risk of material misstatement and that auditors mitigate this risk by performing additional work (Gaynor, Kelton, Mercer, and Yohn 2016). Therefore, if *NEG_MEDIA* is, in fact, reflective of the risk of material misstatement and an auditor does not increase its effort (e.g., increase hours, use higher level labor, hire specialists, etc.), *NEG_MEDIA* will be positively associated with the outcome variables. To examine this possibility, we repeat the analysis in Table 2.10, Panel A within firm-year observations where audit fees do not increase. Panel B presents results of this analysis and again shows no significant association between *NEG_MEDIA* and any of the outcome measures. In sum, even when auditors do not increase their effort, financial reporting failures do not increase. These results provide some evidence that our main findings are not driven by the risk of material misstatement.

Impact on Audit Delay

Client negative media coverage could lead to delays in the audit if it is indicative of additional risk of material misstatement, which would require increased effort (Ettredge, Li, and Sun 2006). We conduct analysis examining the impact of client negative media coverage on audit report delays. For this analysis, negative media coverage is measured during the last quarter of *t* and the first quarter of *t*+1, which reflects the period during which risk could cause auditors to delay signing and releasing the report due to the need to adjust procedures. *AUDITREPORTLAG* is measured as the number of days between the fiscal year end date and the audit report date minus the SEC's filing deadline requirement (60, 75, and 90 days for large accelerated, accelerated, and non-accelerated filers, respectively) (Hoitash and Hoitash 2016). We do not detect an association between negative media coverage during this period and *AUDITREPORTLAG* (untabulated). This suggests that when coverage peaks during the period in which the auditor releases their report, they do not increase effort to the extent that delays the release of the audit report. This is inconsistent with a risk of material misstatement explanation and provides further support for a fee premium/reputation explanation.

Correcting for Potential Selection Bias

Since not all Compustat firms are covered by RepRisk, there is potential that selection bias is influencing our results (i.e., firm characteristics that determine coverage in the RepRisk database also influence dependent variables). In untabulated analyses, we empirically control for a potential selection bias issue through Heckman correction (Heckman 1979). To do so, we use a two-stage model, wherein the first stage we estimate the likelihood of being covered in the RepRisk database (i.e., receiving negative media coverage) as a

function of size and performance controls, as well as dummies for the state of incorporation. These indicators serve as instrumental variables as they are not present in the second stage model, where we use the inverse Mills ratio to control for selection bias in our auditor change audit and audit fee models. Findings are consistent with our main results.

V. DISCUSSION AND CONCLUSIONS

Despite the importance of reputation to an audit firm, there is limited evidence of auditor reputation risk as a contributing factor to an auditors' risk response. In this study, we explore auditors' pricing and client retention strategies in response to client negative media coverage. We present new data, which has not been used in the accounting literature, that quantifies negative media coverage of environmental, social, and governance activities. We argue that reputation damage from this coverage can spill over to impact an auditor's reputation and that auditors are likely to respond to protect their reputation. In contrast, since these activities do not directly relate to audit risk, it is possible that the auditor will not react at all.

Consistent with our predictions, this study provides some of the most direct evidence to date of auditor reputation risk being an important risk consideration for external auditors. Using a large longitudinal sample of U.S. public companies from 2007 to 2014, we find that client negative media coverage is positively associated with the likelihood of auditor change and audit fees. We attribute this reputation effect to the salience of ESG news in modern media and the consequences an audit firm could face from their associations with risky clients. We conduct supplemental analyses to illustrate that the response detected is incremental to that explained by an auditor's traditional risk

considerations. It appears that reputation risks can be egregious enough for auditors to react through both avoidance and sharing channels even when financial risk and the risk of material misstatement are not impacted.

We also find that the impact of client negative media coverage on auditor response is not homogenous. Specifically, results suggest that auditors are more likely to depart in response to the negative coverage of governance issues. This is consistent with media dependency theory, under which stakeholders are likely to have a differentiated dependency on dimensions of corporate reputation. Einwiller et al. (2010) theorize that stakeholders are more dependent on the news media to learn about attributes of a firm's reputation that are important to them. Conversely, coverage of environmental, social, and governance issues are all positively associated with audit fees, suggesting that audit fees are a mechanism to share many risk burdens with the client.

Our study has several limitations. First, we are limited in interpreting our finding for audit fees due to the archival nature of our data. Without data on actual audit hours and billing rates, we cannot measure directly whether an auditor increases effort or charges a premium in response to client negative media coverage. Despite conducting a battery of supplemental analyses, including multiple that utilize monthly data to separate premium and effort explanations, we still admit this shortcoming and leave the question for future research. Second, we present comprehensive evidence of auditor response to client negative media coverage, but do not examine positive media coverage. Using *Fortune's* Most Admired List to measure reputation, Cao, Myers, and Omer (2012) find that positive aspects of company reputation are associated with higher-quality financial reporting. Given

this finding, future research may consider if positive reputation characteristics insulate a company and its related parties from damage following risky events.

Overall, the findings in this study suggest that auditors incorporate client negative media coverage in their decisions. Managers should consider that consequences of environmental, social, and governance-related practices can extend beyond their direct costs, and that related parties such as the auditor are incorporating this information in their decision-making. These results should motivate future research to consider further risk factors independent from the risk of material misstatement that are incorporated into audit pricing and retention decisions.

Part Three

Negative Media Coverage of Environmental, Social, and Governance Practices and CEO Dismissal

I. INTRODUCTION

This study examines negative media coverage of environmental, social, and governance (ESG) practices as a determinant to CEO turnover events.[58] The board of directors is responsible for turnover decisions, and understanding board sensitivity to ESG issues is important given the rising expectation that companies "do good while doing well" (i.e., create a positive impact while maintaining a healthy bottom line). Reflective of this, recent media scrutiny of company actions extends beyond financial performance (e.g., Deloitte 2014; Medland 2016). For example, Target was subject to public criticism surrounding an expansive breach of customer information in 2013 (Sidel, Yadron, and Germano 2013). Similarly, Volkswagen has been under fire for rigging emissions tests on millions of vehicles (Russell, Gates, Keller, and Watkins 2016). In these two high-profile cases, coverage of ESG issues resulted in CEO turnover. However, boards of other companies facing similar criticism have not dismissed their CEO (e.g., Monsanto and Johnson & Johnson). Thus, despite a rising demand for oversight of ESG issues (e.g., GSIA 2014), it is unclear whether, on average, CEOs of companies attracting negative media coverage for their ESG practices are significantly disciplined.

Surprisingly, there is very little research examining executive turnover following ESG issues, including media coverage of these issues. To the best of my knowledge, there are no studies that examine turnover resulting from an aggregate measure of ESG issues, from environmental or social issues, nor from coverage in a diverse range of media sources. The identified gaps in the literature motivate the current study, which seeks to understand

[58] As measured in this paper, environmental issues surround those related to a company's environmental footprint, such as pollution, overuse of resources, waste issues, and more. Social issues include community and employee relations issues such as human rights, discrimination, and labor issues. Governance issues include corruption, executive compensation, anti-competitive practices, and more.

whether corporate boards hold CEOs accountable for ESG-related coverage in a broad range of media sources.

Prior studies find an increased likelihood of CEO turnover following media coverage of declining financial performance and financial misconduct, asserting that negative publicity pressures corporate boards to consider corrective action (e.g., Efendi, Files, Ouyang, and Swanson 2013; Farrell and Whidbee 2002, etc.). Yet, is not obvious whether boards heed to this pressure when it stems from ESG issues. A CEO's primary objective is to deliver economic returns to shareholders (Murphy and Zimmerman 1993) and it is oft-debated whether ESG investment adds or detracts from this objective (Margolis, Elfenbein, and Walsh 2009). Thus, ESG practices may not play an important role in CEO evaluation. Further, recent literature finds that negative media coverage can be "sensational" (i.e., to provide entertainment value) and fail to cause the sort of change one would expect (e.g., Chen, Powers, and Stomberg 2015; Core, Guay, and Larcker 2008). If negative coverage of ESG practices is merely sensational, boards may deem it unnecessary to hold CEOs publicly accountable. This may be particularly true for coverage of ESG practices, wherein the media is able to choose which activities and companies to cover since there are limited other sources for this information (Kolbel, Bush, and Jancso 2017). In these ways, it is possible that boards behave differently in response to coverage of ESG issues than to coverage of financial performance issues.[59]

Alternatively, regardless of its content, negative media coverage is likely to expand the visibility of issues (Rhee and Valdez 2009), increase reputation risk (Fombrun and

[59] More specifically, information on financial performance is available via a variety of mediums (e.g., web searches, company-issued reports, etc.). Therefore, it is unclear whether findings from studies that show a positive association between CEO turnover and media coverage of declining financial performance and financial misconduct (e.g., Efendi et al. 2013; Farrell and Whidbee 2002) will hold in my setting.

Shanley 1990), and cause decision-makers to take corrective action (Bednar, Boivie, and Prince 2013; Joe, Louis, and Robinson 2009). Since CEOs bear responsibility for oversight regardless of their involvement, I predict that boards will be more likely to remove their CEO when facing negative media coverage of ESG practices.

My sample consists of 9,027 firm-year observations from 2007-2015. RepRisk data is used to uniquely measure negative media coverage relating to ESG issues. RepRisk is a business intelligence provider that automatically collects coverage of 28 ESG issues on a daily basis. Automatic collection allows for comprehensive coverage of a diverse range of media sources, which are varied in their prominence (e.g., social media, blogs, major print media, etc.). Collected data is aggregated into a continuous index using a proprietary algorithm that incorporates the identified issues, as well as the severity of the issues (i.e., their consequences, extent, and cause) and the reach of media sources in which they are identified (i.e., low reach such as a blog, or high reach such as the Wall Street Journal). This index and indicator variables for the existence of issues in each category serve as my primary test variables. To identify CEO succession events, initial data is collected from Audit Analytics' Director and Officer Changes dataset, which compiles turnover event information as reported in 8-K filings. To focus solely on dismissals, I supplement this with hand-collected data on the reason for CEO turnover as cited in the popular press.[60]

Overall, findings support the prediction that negative media coverage of ESG practices impacts CEO turnover events. Specifically, I find a positive association between aggregate ESG coverage, as well as individual environmental and governance categories, and CEO dismissal likelihood. This finding suggests that ESG issues do make their way

[60] Firm-year observations with a voluntary CEO turnover (i.e., one due to retirement, death, for a position elsewhere, with individual remaining on the board, etc.) are removed from the sample for all analyses.

into the boardroom when they are covered by the media and on average increase the likelihood that CEOs will be held publicly accountable. Consistent with the prediction that media coverage elevates the importance of ESG issues to board decision-making, I find that for all three categories (i.e., environmental, social, and governance), it is only when issues are covered by high reach media sources that CEO dismissal is more likely.[61] Thus, firms could have severe ESG issues, but if they aren't highly publicized, then it does not appear that the CEO is forced out. This supports the theory that media coverage of these issues prompts boards to remove their CEOs.

I conduct additional analyses to examine the association between negative media coverage and CEO dismissal. First, I find that negative media coverage of environmental and social practices has a greater impact in a sample of companies held by two popular ESG-focused funds. Second, I find that boards that have a committee to oversee sustainability issues are more likely to dismiss their CEO following coverage of environmental and social issues. These two findings suggest boards that are sensitive to ESG issues, via additional monitoring by ESG-conscious institutional ownership or a board-level sustainability committee, are less tolerant of environmental and social criticism. Conversely, I find that larger and busier boards are less likely to remove their CEO following negative coverage of governance issues, which is consistent with lower board monitoring quality. Lastly, I find that results are insensitive to financial performance (i.e., interactions between media measures and measures of financial performance are not significant). This partially addresses concerns that my results are solely driven by ESG issues that harm financial performance.

[61] High reach media sources include international media such as Financial Times, New York Times, and Wall Street Journal, as well as most national and regional media.

Following CEO dismissal, the optimal replacement strategy is unclear. Recent anecdotes highlight that boards of troubled companies are criticized if they do not choose an external candidate. For example, Volkswagen's choice to hire an internal candidate with 40 years of experience at the company despite the assumed pervasiveness of their emissions rigging scandal launched a torrent of media criticism (Boston 2015). Interestingly, whether media coverage influences the choice of CEO successor has not been examined by prior literature. CEO successors are most commonly selected internally (Booz and Company 2011; Conference Board 2016) and are valued due to their firm-specific knowledge (Agrawal, Kboeber, and Tsoulouhas 2004; Datta and Guthrie 1994). In contrast, external candidates are often hired following misconduct or missed performance expectations due to the perception that they can change firm policies and strategies (Farrell and Whidbee 2003; Gangloff, Connelly, and Shook 2016). Therefore, within firms that dismiss their CEO, I predict that negative media coverage of ESG practices is positively associated with the likelihood of an external replacement. Surprisingly, I do not find support for this prediction. I do, however, find that this association exists in the governance category. Combined, these findings suggest that boards do not believe that environmental and social issues warrant a need to break with former policy, but that governance issues are more likely to tarnish reputations and abilities of internal candidates.

I also examine changes to negative media coverage following CEO dismissal and successor choice. It is an open question whether criticism will decline following a turnover event. The board is seemingly removing the CEO to achieve that task (Gangloff et al. 2016). However, negative media coverage may be endemic to a firm and persist even after an executive is held accountable. Further, it is unclear whether either replacement type will

be able to fend off media criticism. While insider replacements are seen as valuable due to their firm-specific knowledge, they may be blinded by an established view of the company and unable to break from prior policy (Agrawal et al. 2004). An external replacement is seen as better able to break with former policies, but also needs to gain firm-specific knowledge before enacting change (Shen and Canella 2002). Interestingly, I find that negative media coverage declines when boards decide to replace the CEO, but that the successor's origin (i.e., external or internal) does not differentially impact future criticism. Therefore, the conventional wisdom that external successors are necessary following criticism is not supported in this setting.

This study makes several contributions to the literature. First, I contribute to literature on how corporate boards respond to negative media coverage. I do so using data that comprehensively captures media coverage of ESG issues in a variety of mediums, which extends research that examines the media's role in corporate governance (e.g., Dyck and Zingales 2002; Dyck, Volchkova, and Zingales 2008). Interestingly, findings suggest that highly publicized ESG issues do garner boardroom attention. To the best of my knowledge, this is the first study to document several determinants of CEO turnover, including an aggregate ESG measure, environmental and social issues, and coverage in a diverse range of media sources. Second, I provide evidence that boards that are sensitive to ESG issues are more likely to dismiss their CEO when facing negative media coverage, and particularly take environmental and social criticism more seriously. Third, findings of this study contribute to extant research on the association between CEO turnover, characteristics of the replacement executive, and subsequent improvement to the original determinants of turnover (e.g. Francis, Huang, Rajgopal, and Yang 2008; Li, Sun, and

Ettredge 2010). Specifically, negative media coverage is associated with CEO dismissal likelihood and CEO dismissal leads to a decline in negative coverage. Lastly, results contribute to the open debate of insider versus outsider replacement in executive succession events (e.g. Karaevil and Zajac 2012; Boston 2015). While the media pushes boards to choose external successors, it does not appear that boards placate this demand or that it matters for fending off media criticism. Practically, this study provides directors and other interested stakeholders (e.g., investors, activists, auditors, etc.) information about CEO succession that could prove useful when facing negative media coverage.

II. BACKGROUND AND HYPOTHESES DEVELOPMENT

Negative Media Coverage of ESG Practices

Negative media coverage is likely to shape public opinion. In fact, the agenda setting paradigm highlights that the media, through its packaging and rebroadcasting role, are successful at forming public opinion and specifically, can raise the salience of certain issues in the public's agenda (Carroll and McCombs 2003; McCombs and Shaw 1972). The more a story or issue is publicized, and therefore disseminated to parties that may be otherwise unaware of it, the more likely the public will label it as important. The media is thus an indicator of the public's knowledge (Deephouse 2000) and is actively involved in influencing public concerns. Prior media studies in the business literature most commonly collect coverage from major international news outlets (e.g., Bednar 2012; Christensen 2016). However, in today's corporate environment, companies face growing concerns about the consequences of negative media coverage in a wide variety of information sources (e.g., social media, blogs, online news, etc.) (Deloitte 2014). These less prominent sources also influence public opinion (Carter and Bos 2017).

This is evident in recent anecdotes, where the media creates and disseminates information about the environmental, social, and governance (ESG) practices of public companies. Scrutiny of public companies extends beyond financial performance (Medland 2016). The media widely reports on company scandals and other misgivings. For example, the Deepwater Horizon oil spill, the largest accidental release of oil into public waters, launched a torrent of public criticism at BP that still lasts seven years later (e.g., Allen 2012). Environmental issues include pollution, overuse of resources, animal mistreatment, and more. In another example, Apple attracted negative media attention for their use of child labor in 2009. Criticism of social practices such as this extend beyond child labor to include poor employment conditions, human rights abuses, discrimination, and health and safety issues. Governance issues include corruption, bribery, misleading communication (e.g., greenwashing), anti-competitive practices, and more. ESG issues reflect problems that are likely to encompass both competence and integrity, and the coverage of these issues may prove influential to both public opinion and company decision-making.

The media may be particularly powerful at influencing public opinion on ESG issues because there are limited sources of other information about these practices (e.g., Aerts and Cormier 2009). Specifically, information on irresponsible practices is often created by external observers and distributed by the media (Kolbel et al. 2017). While various forms of non-financial reporting exist that may also provide this information, these voluntary company-issued reports are more prone to contain positive information about ESG practices than negative (Kolbel et al. 2017). This reporting is also still in its infancy and because it is voluntary, there are concerns over the transparency and credibility of

information (Huang and Watson 2015). Further, the public in general is more likely to access and be influenced by daily media than a company-issued report.

Negative Media Coverage and CEO Dismissal

Given the prevalence and prominence of ESG criticism, potential damages associated with negative media coverage can cause firms to take action to protect reputation (e.g., Bednar et al. 2013; Chen et al. 2015; Dhaliwal, Goodman, Hoffman, and Schwab 2016). One particularly intuitive consequence of negative media coverage of ESG practices is executive turnover, yet academic research at this intersection is limited.

In contrast, research in the broader field of executive accountability is extensive and includes evidence of an increased likelihood of CEO turnover following poor performance (Coughlan and Schmidt 1985; Huson, Malatesta, and Parrino 2004; Jenter and Kanaan 2015; Karaevli and Zajac 2012; Murphy and Zimmerman 1993; Weisbach 1988). Additionally, top executives of firms that restate their earnings or issue inaccurate management forecasts experience more turnover than executives of control firms (Arthaud-Day, Certo, Dalton, and Dalton 2006; Desai, Hogan, and Wilikins 2006; Gangloff et al. 2016; Land 2012; Lee, Matshunaga, and Park 2012), and this is likely done to repair organizational legitimacy (Feldmann, Read, and Abdolmohammadi 2009). A few of these studies examine media coverage of these issues. For instance, Agrawal, Jaffe, and Karpoff (1999), Farrell and Whidbee (2002), and Efendi et al. (2013) associate CEO turnover with Wall Street Journal coverage of fraud, poor performance, and option backdating, respectively. These studies claim that negative publicity pressures boards to consider corrective action by holding the CEO publicly accountable.

Prior literature has not examined whether the finding that CEO turnover follows media coverage of financial issues holds true for ESG issues. Specifically, it is unclear whether, on average, CEOs are dismissed following media coverage of ESG issues.[62] Given that a CEO's primary objective is to deliver economic returns to shareholders (Murphy and Zimmerman 1993), it is not surprising that they are held accountable for media coverage of declining financial performance and financial misconduct (e.g., Efendi et al. 2013; Farrell and Whidbee 2002). However, prior literature finds inconclusive evidence for the impact of ESG investment on financial performance (Margolis et al. 2009). Thus, if a company is performing well financially, issues such as pollution and human rights may be considered as lower priority and not play a role in CEO evaluation. Further, recent studies have shown that media coverage can be "sensational" and fail to cause the sort of change one would expect. Chen et al. (2015) find that firms do not decrease tax avoidance in response to negative media coverage of the practice, but rather decrease disclosure readability as a means to curtail media attention. Similarly, Core et al. (2008) do not find that CEO turnover increases or CEO pay decreases following negative coverage of CEO pay. If media coverage of a company's ESG issues is merely sensational, a company may deem it unnecessary to hold the CEO accountable, and pursue corrective action in other ways. For these reasons, it is possible that CEOs are not held accountable for ESG issues.

[62] Two recent studies examine a construct related to ESG, using aggregate activity-based measures of corporate social responsibility (CSR). Chiu and Sharfman (2016) find that corporate social irresponsibility is positively associated with CEO turnover likelihood, and Hubbard, Christensen, and Graffin (2017) find that investments in CSR amplify the association between financial performance and CEO turnover likelihood. These studies did not examine media coverage of these issues, nor did they disaggregate the construct into ESG-related components.

Alternatively, there are viable arguments that a CEO dismissal would follow negative media coverage of ESG practices. As the highest-level executive, a CEO bears responsibility for organizational decisions and actions, including a company's vision, strategic direction, policies, and culture (Flatt, Harris-Boundy, and Wagner 2013). Although it is impossible for CEOs to make all decisions within a company, they are positioned in an oversight role and can be held responsible for decisions and actions at all levels (e.g., Deloitte 2014; Farrell and Whidbee 2002). Recently, companies are expected to create value for both shareholders and stakeholders (Porter and Kramer 2011), which requires monitoring of both financial and ESG issues. Therefore, following negative media coverage of ESG practices, directors may be more likely to dismiss executives to show investors and other stakeholders that they are sensitive to these issues. This action is a form of blame assignment or scapegoating, and can help to mitigate negative reactions following misconduct (Gangloff et al. 2016; Shapiro 1991).

To the best of my knowledge, there are no studies that examine turnover following coverage of environmental or social issues. There are, however, four studies that associate negative media coverage of governance issues, as published in a specific or limited set of news outlets, with the likelihood of CEO turnover. Wu (2004) finds that companies are more likely to change their CEO after being publicly named by CalPERS (i.e. the largest state pension fund in the U.S., which is known for promoting good corporate governance) for having poor corporate governance practices. Similarly, Joe et al. (2009) find that firms listed on Business Week's worst board list are forced to take corrective actions, which include CEO and board chairman replacement and an increase in independent directors. Bednar (2012) detects a significant response to negative coverage of corporate governance

issues (e.g., executive pay and management philosophy) in six major media outlets. In contrast, Core et al. (2008) do not find that CEO turnover increases in response to negative media coverage of CEO pay. Thus, in addition to documenting responses to coverage of environmental and social issues, I also seek to extend findings of these governance studies to an aggregate ESG measure, a more comprehensive set of media outlets, and to a broader sample.

Guided by the cited findings that CEO turnover increases following negative coverage of governance issues, as well as recent anecdotes of CEO turnover following highly publicized ESG events, I predict that boards will hold CEOs accountable for both overall negative media coverage and coverage of specific ESG events in H1 and H2, respectively:

> **Hypothesis 1:** Negative media coverage is positively associated with the likelihood of CEO dismissal.
>
> **Hypothesis 2:** Negative media coverage of environmental, social, and governance issues are all positively associated with the likelihood of CEO dismissal.

Negative Media Coverage and CEO Successor Origin

With CEO turnover comes CEO replacement. Effective succession planning is an important duty of the board of directors, as they are tasked with identifying the candidate that can meet the business' current and future needs (e.g., Zhang and Rajagopalan 2004). When selecting a new CEO, a firm can appoint an inside successor, or it can appoint an outsider. This decision can be critical for subsequent operating performance (Dalton and Kesner 1985). Recognizing this, several studies examine the choice between appointing an insider or outsider (e.g., Borokhovich, Parrino, and Trapani 1996; Farrell and Whidbee 2003; Gangloff et al. 2016; Shen and Cannella 2002).

Generally, boards appoint insider replacements to provide continuity. Surveys show that insiders are chosen as replacement CEOs around 80 percent of the time (Booz and Company 2011; Conference Board 2016). In fact, insiders are often identified as CEO succession candidates before turnovers occur and are groomed for the role by serving as high-level executives until their succession (EY Center for Board Matters 2014). This succession strategy is known as the "pass the baton" method (Naveen 2006). Strategies like this are recognition that insiders benefit from possessing firm-specific knowledge such as familiarity with products, markets, technologies, and standard operating procedures (Agrawal et al. 2004; Datta and Guthrie 1994). Additionally, hiring an insider avoids adverse selection issues that may be at play when selecting an outsider based on limited knowledge of their abilities (Shen and Cannella 2002). Despite these strengths, an insider CEO replacement following negative media coverage may be considered "scapegoating." Scapegoating is a largely symbolic action designed to placate demands for change following misconduct without disrupting the continuity of company operations (Gangloff et al. 2016). Replacing the CEO with an insider appeases public criticism by attributing fault to an individual (i.e., the former CEO), but may not introduce real change to address the misconduct. This solution effectively blames a single person, the former CEO, for misconduct that likely permeates throughout the firm and its culture, which the insider replacement is a part of.

Conversely, hiring an outsider as CEO replacement is a means to signal to investors and other stakeholders about a firm's intent to change future behavior (e.g., Agrawal et al. 1999; Farrell and Whidbee 2003; Gangloff et al. 2016). Top management brought in from outside the firm are thought to have broad, fresh perspectives and an ability to implement

change to firm policies and strategies (Farrell and Whidbee 2003; Gangloff et al. 2016). This is evident in the recent events at Target and Volkswagen, where the mainstream media questioned the latter's choice of an insider replacement and the potential inability to break from misconduct culture (Boston 2015). Whether there is truth to the signal or not, it may be necessary to hire an outsider successor in situations where stakeholders do not believe that insiders can bring desired change. This is documented in prior literature, in which evidence is presented consistent with boards selecting outsiders following poor performance or when the external environment is changing (e.g., Huson et al. 2004; Parrino 1997). Following misconduct, firms may wish to communicate their intent to change the tone at the top and to alleviate concerns of the misconduct occurring again (Karaevli and Zajac 2012). The selection of an outside successor acknowledges that misconduct is pervasive and signals to internal and external stakeholders of the firm that the board is serious about change (Datta and Guthrie 1994). However, it is important to note that struggling companies may have difficulty attracting a suitable external replacement because these individuals may not want to take control of a failing organization (Dalton and Kesner 1985).

In sum, insider CEO replacements are thought to bring continuity and not disrupt current organizational processes and culture, whereas outsider CEOs are often hired to signal willingness to change in response to misconduct. Thus, while insider replacements are most frequent, there is reason to believe this will not be the case when dismissal occurs following negative media coverage. Specifically, the impact of negative media likely extends beyond CEO control to impact the reputation of otherwise viable insider candidates. It may be perceived that the ties of insiders to the culture which prompted

negative media coverage complicate efforts to change, whereas an external CEO is perceived as bringing a fresh perspective to operations and culture. This has not yet been empirically examined, and it is thus unknown whether findings that external CEO replacement follows poor performance are generalizable to media coverage or to ESG issues. ESG issues may be seen as less important, and in their presence a trade-off decision between breaking with former policy to correct ESG issues (i.e., appointing an outsider) and maintaining operational and cultural norms (i.e., appointing an insider) must be made. Additionally, ESG issues may not permeate a firm's culture to tarnish the reputation of otherwise viable insiders in the way that financial misconduct does. However, based on prior literature and recent scrutiny of companies that hire external replacements following an ESG incident, I hypothesize that firms with negative media coverage will be more likely to appoint an outsider in order to send a signal of a clean break with failed policies and strategies. I predict this in my third hypothesis.

Hypothesis 3: Negative media coverage is positively associated with the likelihood of hiring an external CEO replacement following a dismissal.

Change in Negative Media Coverage

It is also fruitful to consider the alleviation of negative media coverage contingent on the CEO turnover and replacement decision. Examining post-turnover negative media coverage is beneficial because to the extent that media coverage is firm specific, any change between the prior CEO and the new CEO regimes can be attributed to change in media coverage associated with the new CEO regime. Prior literature has found that following a negative event (e.g., a restatement), firms that dismiss top management recover faster than firms that do not (e.g., Wilson 2008). This supports the notion that executive dismissal signals that directors are adequately addressing issues, and that blame assignment

of this sort helps to mitigate negative reactions following misconduct (Gangloff et al. 2016; Shapiro 1991).

In this setting, CEO dismissal may be a necessary step to fend off media criticism. If the media digests the dismissal signal consistent with blame assignment/scapegoating logic, then negative coverage will decline. If CEO dismissal occurs following negative media coverage, there is likely an expectation that the replacement CEO will prioritize repairing the situation that led the former CEO to leave. However, if the board is merely turning over their CEO to appease public opinion, the replacement CEO may not take actual steps to change company practices and this could result in continued or additional negative coverage. Further, negative media coverage may be endemic to a firm and persist even after the CEO is forced out.

The choice of CEO successor is also likely to impact changes in media coverage. However, prior literature documents mixed findings for the effectiveness of internal and external replacements. Insider CEOs are generally seen as more able than outsiders as they have acquired firm-specific knowledge and relationships (Agrawal et al. 2004). Survey data has supported this, illustrating that shareholder returns of companies with insider replacement CEOs outperform those with outsiders (Booz and Company 2011). However, in misconduct scenarios, an insider hire may be blinded by an established view of the company and unable to break with culture and lead the firm in its recovery. An outsider will need to gain firm-specific knowledge (e.g., the people and their skills, the objectives and prospects, etc.) before embarking on major changes, which can slow down repair. Further, when selecting an outsider replacement, the board of directors has limited

information, which may make the selected individual the incorrect choice to guide the firm in its recovery (Shen and Cannella 2002).

In sum, it is not clear whether CEO dismissal nor either successor type will result in a decline in negative media coverage. In fact, if the media sees through the CEO dismissal signal, the successor does not enact proper change, or the negative coverage is endemic to the firm's environment, it may increase following dismissal. Given these competing arguments, I present hypotheses for the change in negative media coverage in their null form:

Hypothesis 4: CEO dismissal is not associated with the change in negative media coverage.

Hypothesis 5: Firms that hire external CEO replacements do not experience greater declines in negative media coverage than those who hire an internal replacement.

III. DATA AND METHODOLOGY

Sample

My sample consists of 9,027 firm-year observations with necessary coverage in several databases from 2007 – 2015.[63] The yearly distribution of this sample can be found in Table 3.1. Data on negative media coverage of ESG practices is gathered from RepRisk. Audit Analytics' Director and Officer Changes dataset is used to identify turnover events and is supplemented with hand-collected data on the reason for turnover. Lastly, Compustat, BoardEx, and CRSP contain necessary control variable data.

[INSERT TABLE 3.1 HERE]

Variable Definitions

Measuring CEO Dismissal and Successor Origin

[63] RepRisk coverage begins in 2007, so the chosen sample period represents all available data.

Audit Analytics aggregates data on director and officer changes, which is collected from Item 5.02 of 8-K filings with the SEC. The dataset provides the date of CEO turnover events, along with the name of the departed and successor CEO and the type of CEO turnover event (e.g., deceased, dismissed, retired, etc.). These events include both voluntary (e.g., retirement) and forced (e.g., dismissal) turnovers. In accordance with predictions that CEOs are forced out following negative media coverage, it is important that I capture only dismissals.[64] Therefore, I manually search for news articles discussing each turnover event identified by Audit Analytics. Following Campbell, Gallmeyer, Johnson, Rutherford, and Stanley (2011), I classify a CEO turnover as a dismissal if it is described as such in a news article, or if the following four criteria are met. These criteria are: (1) turnover was not announced at least six months in advance of the turnover date, (2) departing CEO does not leave for reasons of poor health, death, or to accept a position elsewhere, (3) departing CEO is under the age of 60 and thus less likely to be retiring, and (4) departing CEO does not remain on the board of directors after leaving the CEO position.[65] In order to cleanly separate treatment and control observations, I remove firm-year observations with voluntary CEO turnover from the sample.

[64] This is in contrast to using a dependent variable that captures all turnover events, which would include those related to death and retirement, amongst other reasons. There are many turnover events identified by Audit Analytics that are clearly voluntary events, and should not be associated with negative media coverage. For instance, in 2010 Domino's Pizza CEO David Brandon left his post to become the athletic director at University of Michigan (Stynes 2010). Based on the criteria outlined for forced turnover classification, this turnover event is classified as voluntary because it is to accept a position elsewhere.

[65] Hand collecting this data is imperative because 21.07% of CEO turnovers that I initially identified as voluntary from the Audit Analytics dataset (i.e., because turnover action was listed as retired, personal leave, etc.) are classified as forced based on the listed criteria. For example, in 2012 Best Buy's CEO Brian Dunn "resigned," which would suggest a voluntary turnover. However, the turnover was announced abruptly (i.e., the same day) and most importantly, was discussed in multiple news articles that clearly suggest that Dunn was forced out due to personal conduct issues (e.g., Bustillo 2012).

CEO_DISMISSAL is an indicator variable equal to one if the CEO is dismissed during the fiscal year, and zero otherwise. Data on the employment history of successor CEOs is gathered from BoardEx. Following prior literature, I classify CEO successors with less than one year of tenure in the firm as external replacements (*EXTERNAL_CEO*). CEO successors who were employed by the firm for more than one year before the appointment are classified as internal replacements (*INTERNAL_CEO*).

Measuring Negative Media Coverage

Data on negative media coverage is gathered from the RepRisk database. RepRisk contains various measures of negative media coverage of ESG issues. The database aggregates over 80,000 external media sources into composite metrics.[66] RepRisk focuses on selectively collecting criticism or negative news related to 28 ESG issues. Artificial intelligence is used to collect coverage of these issues from a variety of sources (e.g., major print media, newsletters, news sites, blogs, social media, etc.). Trained analysts then verify and analyze the data.

RepRisk analysts use a proprietary algorithm to compile issue data into a monthly index that measures negative media coverage of ESG practices. The algorithm is based on the identified issues, the severity of the issues (i.e., their extent, cause, and consequences),[67]

[66] Referenced prior literature has used databases that allow access to individual news stories to collect media coverage. For example, Christensen (2016) use the Factiva database to collect high-profile misconduct incidents from a pre-selected group of media sources. Chen et al. (2015) also use Factiva to search for articles in eight influential news sources (Wall Street Journal, Barron's, Forbes, Financial Times, New York Times, Washington Post, Chicago Sun-Times, and USA Today). To the best of my knowledge, Kothari, Li, and Short (2009) have the broadest collection of media sources. The authors use Dow Jones Interactive and Factiva to examine more than 400 sources.

[67] The extent of the issue is based on the number of people impacted (e.g., one person, a group of people, a large number of people). The cause of the issue is based on whether it was caused by an accident, negligence, or intended. The consequences of the issue include no further consequences, injury, death, etc.

the reach of media sources issues are identified in,[68] and the frequency and timing of this information. This index is well suited to examine CEO dismissal in response to negative media coverage since it adjusts for the reach of the media source. Specifically, theory suggests issues that garner attention from high reach sources (e.g. Wall Street Journal or New York Times) are likely to be more salient to the public and cause firms to consider top management turnover in crisis management discussions.

To merge RepRisk with necessary dependent and control variables, I annualize the monthly data provided. The primary test variable is *NEG_MEDIA*, which is measured as the maximum index of negative media coverage within a specified period. For firm-years that do not have a CEO dismissal, I take the maximum in each fiscal year.[69] For firm-years that do have a CEO dismissal, I take the maximum within the year (i.e., twelve months) prior to the turnover date. A graphical depiction of variable timing can be found in Figure 3.1. In this figure, the measurement timing for *NEG_MEDIA* is shown above the timeline. For treated observations, it is illustrated that the maximum index is taken in the year preceding the turnover date, rather than the fiscal year as illustrated for untreated observations.[70] I also create three indicator variables for the coverage of an issue in each of the following categories: environmental (*E_ISSUE*), social (*S_ISSUE*), and governance (*G_ISSUE*). These variables are equal to one if a firm-year observation has a granular issue within the respective broad category, and zero otherwise.

[INSERT FIGURE 3.1 HERE]

[68] The reach of media sources is a pre-classified determination. High reach media sources include international media such as Financial Times, New York Times, BBC, etc. In this study, I collapse medium reach media sources with this category; these include most national and regional media. Low reach media sources include local media, blogs, internet sites, etc.

[69] In this study, it is appropriate to use the maximum index because the board is likely to react to peak risk, rather than average risk.

[70] Results are consistent if alternative time periods are used.

Control Variables

In all multivariate analyses, I control for factors shown to impact the likelihood of CEO turnover in prior research (e.g. Borokhovich et al. 1996; Huson, Parrino, and Starks 2001, etc.). For firm-year observations with a CEO dismissal, all independent variables, other than those described above as being annualized from RepRisk's monthly data, are measured during the fiscal year with the closest year-end to the turnover date. This timing is consistent with prior turnover studies. For firm-year observations without a CEO dismissal, all control variables are measured contemporaneously. Figure 3.1 depicts this timing below the timeline.

I expect poorly performing companies to be more likely to dismiss their CEO, and include *ROA* and *STOCKRETURN* as controls and expect a negative sign for both. I also expect departing CEO age (*CEO_AGE*) to be positively associated with the likelihood of CEO dismissal. Further, I control for firm size (*LNASSETS*) and complexity *(SEGMENTS)* (Huson et al. 2001). Since the board makes turnover decisions, I include board characteristics as controls (*BOARD_INDEP* and *BOARD_SIZE*). Lastly, since prior literature has presented evidence consistent with turnover occurring in response to the disclosure of financial reporting failures (e.g., Desai et al. 2006), I control for *RESTATEMENT* and *MW*. All models also include industry (Fama-French 48 industry classifications) and year fixed effects, and standard errors are clustered by firm.

The sample for multivariate analyses testing H3, which utilizes *EXTERNAL_CEO* as the dependent variable, is limited to firms that have a CEO dismissal in year *t*.[71] I predict that some control variables will behave differently in this models. For instance, complex

[71] 11 firm-year observations are dropped from this analysis because I am unable to identify the year the departing CEO joined the company in BoardEx or via hand collection.

firms may have a greater need for firm-specific knowledge and thus, be more likely to hire an internal replacement. I therefore expect *LNASSETS* and *SEGMENTS* to be negative and significant. Two additional controls are included in these models. Specifically, firms with qualified internal candidates may be less likely to hire an outsider (Hoitash and Mkrtchyan 2015). I include controls for *TALENT* (an indicator variable equal to one if there is at least one executive with outside directorships, and zero otherwise) and *HEIR_APPARENT* (an indicator variable equal to one if the firm has a non-CEO president or chief operating officer who has been in the position for less than two years prior to the CEO dismissal, and zero otherwise). Additionally, Fama-French 12 (as opposed to 48) industry classification are used as fixed effects to retain the largest sample possible.[72]

IV. RESULTS

Descriptive Statistics

Table 3.2 displays summary statistics of test, dependent, and control variables (Panel A) and a correlation matrix of key variables (Panel B). *NEG_MEDIA* is on average 14.401. 18.9 percent of firm-year observations in the sample have at least one environmental issue, whereas 25.5 percent have social issues, and 19.4 percent have governance issues. The mean likelihood of CEO dismissal is 3.7 percent, which is 334 firm-year observations. Within these turnover events, the chosen successor is external to the company 34.7 percent of the time.[73] Further detail on the distribution of these turnover events, as well as the distribution of internal and external replacements, is provided in Table 3.1. Descriptive statistics for control variables are consistent with prior literature.

[72] In other words, the Fama-French 48 industry classification drops a significant portion of the CEO turnover sample due its perfect prediction of external CEO replacement.

[73] The frequency of external replacements in my sample is higher than recent practitioner reports suggest (e.g., Conference Board 2016). This is expected because I focus solely on forced turnover events.

[INSERT TABLE 3.2 HERE]

Figure 3.2 graphically displays the monthly mean index value of negative media coverage surrounding CEO dismissal events. Specifically, the mean index value is plotted for each of the 24 months surrounding the CEO turnover date. The graph is powerful as it provides initial results that negative media coverage peaks leading up to CEO dismissal, and that firms that choose external replacements experience a greater peak in coverage. Additionally, the graph illustrates that negative media coverage declines following dismissal for both replacement types.

[INSERT FIGURE 3.2 HERE]

Table 3.2, Panel C provides further information on the distribution of RepRisk's granular data for both treatment and control firms. Specifically, the table displays the frequency of *E_ISSUE*, *S_ISSUE*, and *G_ISSUE* within non-turnover firms, turnover firms, turnover firms that choose internal successors, and turnover firms that choose external successors. Further, each of these issue indicators is broken into buckets based on the severity and reach of the issue. This results in four buckets: (1) issues that are low severity and identified in low reach media sources, (2) issues that are high severity and identified in low reach media sources, (3) issues that are low severity and identified in high reach media sources, and (4) issues that are high severity and identified in high reach media sources.[74] These descriptive statistics illustrate the breadth of RepRisk's collection, as well

[74] Because each of the broad issue categories (i.e., environmental, social, and governance) is made up of several granular issues, it is possible that during a firm-year there could be an issue that is in bucket 2 and another in bucket 4 within the same category. For example, an animal mistreatment issue that is high severity and identified in a low reach media source and a global pollution issue that is high severity and identified in a high reach media source. Because future analysis requires mutually exclusive buckets, I assign these buckets using a hierarchy. For example, following the reverse order of the buckets listed, if a firm-year observation has an issue in the respective category that falls in bucket 4, then it cannot be counted in any lower buckets. This continues through buckets 3, 2, and 1. I note that this hierarchy is subjective. The argument set forth in this paper is that negative media coverage is positively associated with CEO turnover

as the richness of the issue data. Distributions also provide preliminary evidence that ESG issues, and specifically those that are high severity and high reach, are more common for turnover firms than for non-turnover firms. For example, 10.18 percent of turnover firms have a high severity and high reach governance issue, but just 6.80 percent of non-turnover firms do. Further, external appointments are more common for firms with governance issues (27.49 vs. 33.93 percent).

Results of H1 and H2: Negative Media Coverage and CEO Dismissal

To test H1, Table 3.3 presents the results of logit regressions estimating the association of various measures of negative media coverage and the likelihood of CEO dismissal.[75] Each column represents a different measure of negative media coverage. Column 1 suggests that the overall coverage of ESG practices, as measured by *NEG_MEDIA*, is positively associated with the likelihood of CEO dismissal. This finding supports H1.[76] This result is also economically significant. I calculate the economic significance as the change in the likelihood of CEO dismissal when *NEG_MEDIA* moves from the 25th percentile to the 75th percentile. Holding all factors at their sample mean, I observe a 42.95 percent increase in CEO dismissal likelihood.

[INSERT TABLE 3.3 HERE]

events, not the severity of the issue. Thus, I rank issues that are low severity but identified in a high reach media source (bucket 3) as more influential than high severity issues that are identified in low reach media sources (bucket 2).

[75] The sample size reported in all logit models, including this table, is smaller than in the full available sample. This is expected, because observations with perfect prediction of success or failure are dropped from logit model predictions. I partially address this issue by using Fama-French 48 industry classifications, rather than two-digit SIC codes, as industry fixed effects to avoid further dropping of observations due to perfect prediction within a more constrained industry grouping. Results are consistent if two-digit SIC codes are used.

[76] Results in Table 3 are robust to the inclusion of firm (instead of industry) and year fixed effects. However, results of models using industry ad year fixed effects are tabled for consistency with later analyses where it is not possible to use firm fixed effects (i.e., replacement analysis within a sample of CEO turnovers, which has very little within-firm variation).

H2 predicts that negative media coverage of all categories compiled into *NEG_MEDIA* also exhibit positive associations. Column 2 provides evidence in support of H2, with *E_ISSUE* positive and significant. Similarly, Column 4 demonstrates that *G_ISSUE* is positive and highly significant in predicting the likelihood of CEO dismissal. Conversely, Column 3 does not provide evidence in support of H2, as *S_ISSUE* is insignificant. Combined, I find partial support for H2. The impact of coverage of both environmental and governance issues is economically significant. Here, I calculate economic significance as the change in the likelihood of CEO dismissal when the respective issue indicator moves from zero to one. A firm with coverage of an environmental issue is associated with a 29.24 percent increase in the likelihood of CEO dismissal when all other variables are measured at their sample mean. A firm with coverage of a governance issue is associated with a 110.32 percent increase.[77]

It is interesting that the association is weak for environmental issues and insignificant for social issues. This is surprising given the theory that any issue receiving substantial negative press would increase the likelihood of CEO dismissal. Taken as is, results suggest that boards are less concerned about the repercussions of negative coverage of environmental issues than those stemming from governance issues, and are not concerned about negative coverage of social issues. [78] The strong association between coverage of governance issues and CEO dismissal likelihood is consistent with the logic that these issues are reflective of problems with the tone at the top, and that the media

[77] It is not surprising that the economic significance of these variables is high since the CEO turnover dependent variable captures a low frequency event. Additionally, the calculation used holds all other variables at their sample mean, when in reality they would likely fluctuate if issues are identified.
[78] I perform coefficient comparison tests and find that governance issues have a greater impact on CEO dismissal likelihood than coverage of both social ($p<0.01$) and environmental ($p<0.01$) issues.

pushes for the highest ranked executive within the problematic culture to be held accountable.

An important feature of RepRisk data is the ability to disentangle the severity of an issue and the reach of the media source in which the issue was identified. Theory, as presented in this study, suggests that negative media coverage of ESG issues pushes boards to remove their CEO, and that this association is not fully explained by the issue underlying the coverage. To test this assumption, I conduct analysis grouping ESG issues based on severity (i.e., extent, cause, and consequences) and reach of media source issues are identified in (i.e., its prominence). Table 3.4 displays multivariate results regressing *CEO_DISMISSAL* on these issue groupings. Columns 1-3 disaggregate environmental issues, Columns 4-6 social issues, and Columns 7-9 governance issues. For simplicity, I describe the test variables in this table related to the environmental category. *HIGH_REACH* is an indicator variable equal to one if the firm-year observation had one or more environmental issues in a high reach media source (e.g., Wall Street Journal, New York Times, etc.), and zero otherwise. Conversely, *LOW_REACH* is an indicator variable equal to one if the firm-year observation had environmental issues that were not identified in high reach media sources, and zero otherwise. *HIGH_SEV* is an indicator variable equal to one if the firm-year observation had one or more environmental issues that are classified as high severity, and zero otherwise. *LOW_SEV* is an indicator variable equal to one if the firm-year observation had environmental issues that were not classified as high severity. Indicators included in the same model are mutually exclusive (e.g., if a firm-year is equal to one for *HIGH_REACH*, then it is equal to zero for *LOW_REACH* in the same column). These indicators are then combined to create four mutually-exclusive buckets within each

issue category (i.e., *LOWSEV_LOWREACH, HIGHSEV_HIGHREACH, LOWSEV_HIGHREACH,* and *HIGHSEV_HIGHREACH*). The creation of these buckets is described earlier in the text, and descriptives can be found in Table 3.2 Panel C.[79]

[INSERT TABLE 3.4 HERE]

Results in Column 1 suggest that the reach of media source that environmental issues are published in does not influence CEO dismissal likelihood. Conversely, results in Column 2 appear to illustrate that the severity of environmental issues is a significant determinant. Specifically, *HIGH_SEV* is positive and significant, suggesting that high-severity environmental issues are positively associated with CEO dismissal likelihood. However, in Column 3, results suggest that it is actually the combination of high severity environmental issues identified in high reach media sources that influence the turnover decision (i.e., *HIGHSEV_HIGHREACH* is positive and significant). Results for social issues, as displayed in Columns 4-6, suggest that severity alone does not matter for CEO dismissal likelihood (Column 5), but rather that the reach of the media source a social issue is published in (Column 4) is driving the decision. Consistent with environmental issues, I further note that it is the combination of high severity social issues identified in high reach media sources that determine the turnover decision (i.e., *HIGHSEV_HIGHREACH* is positive and significant in Column 6).

Results for governance issues follow a different, yet interesting, pattern. Specifically, results in Column 7 suggest that governance issues identified only in high reach media sources influence the likelihood of CEO dismissal, whereas results in Column

[79] As described earlier in the text, to create mutually exclusive buckets, I used theory to rank issues that were low severity and high reach (*LOWSEV_HIGHREACH*) higher than issues that were high severity and low reach (*HIGHSEV_LOWREACH*). Results are consistent if this ranking is switched, which alleviates concerns that results are mechanically driven by the classification order.

8 suggest that CEO dismissal likelihood increases regardless of the severity of a governance issue. When combined, it appears that the reach of media dominates severity in influencing the dependent variable. Specifically, both *HIGHSEV_HIGHREACH* and *LOWSEV_HIGHREACH* are positive and significant. The former is consistent with findings for environmental and social issues, but the latter suggests that for governance issues, even issues that are not severe but are highly publicized, garner boardroom attention

To summarize, results suggest that ESG issues are only positively associated with the likelihood of CEO dismissal when they are covered by high reach media sources. In Table 3.3, it appears that environmental issues are a weak determinant of dismissal and that social issues do not matter at all. However, results in Table 3.4 reconcile this perplexing finding. Specifically, dismissal likelihood is influenced by severe environmental and social issues identified in high reach media, as well as all governance issues identified in high reach media regardless of severity. For all categories, firms could have severe issues, but if they are not highly publicized, then results suggest that the board does not react by holding the CEO publicly accountable. This suggests that negative media coverage of these issues has an incremental impact to that explained by the event that underlies the coverage. This is consistent with the theory that media criticism prompts boards to take action.

Results of H3: Negative Media Coverage and CEO Successor Origin

To test H3, Table 3.5 presents the results of logit regressions estimating the association of various measures of negative media coverage with the likelihood of external CEO replacement, within a sample of firm-year observations that have a CEO dismissal. Consistent with previously presented tables, each column represents a different measure of negative media coverage. Column 1 suggests that overall coverage of ESG practices, as

measured by *NEG_MEDIA*, is not associated with the likelihood of CEO dismissal. Thus, H3 is not supported. It appears that, in aggregate, negative media coverage of ESG issues pushes boards to turnover CEOs, but does not cause them to choose external successors.

[INSERT TABLE 3.5 HERE]

Given limited literature and a priori theory on the topic, I do not formally predict the impact of coverage of individual issues on the likelihood of external replacement. Regardless, models using the *E_ISSUE*, *S_ISSUE*, and *G_ISSUE* indicator variables are also presented in Table 3.5. The only significant determinant of external CEO replacement is *G_ISSUE* (Column 4). It appears that when CEO dismissal occurs, coverage of governance issues positively influences the likelihood of external replacement. This is consistent with the theory that suggests an external replacement is necessary to break with former policies and implement change. Governance issues are likely to permeate a firm's culture and potential insider candidates more than environmental and social issues. Further, directors may believe that the media will see through any scapegoating attempts when facing governance issues. To further explore this result, I again utilize unique data on the severity and reach of media source in which issues were identified. These findings are presented in Table 3.6. Consistent with the main results for H3, there are no significant variables within coverage of environmental and social issues (Columns 1-4), but high severity governance issues are significant (Column 6). I do not report results estimating the impact of issue buckets (i.e., with reach and severity combined) on the likelihood of external replacement because of sample constraints. However, these results suggest that severe governance issues published in high reach media sources are those which drive this association.

[INSERT TABLE 3.6 HERE]

Overall, I do not find support for H3. In aggregate, negative media coverage of ESG issues does not influence the likelihood of an external replacement when CEO dismissal occurs. This is surprising since countless anecdotes exist in which the media criticizes the choice of an internal successor when a CEO dismissal occurs in the wake of ESG issues (e.g., BP, Volkswagen, Wells Fargo, etc.). These findings highlight that, on average, boards are not more likely to hire an external successor even though there will be continued criticism about that choice. However, when this data is disaggregated, firms facing negative coverage of governance issues are more likely to hire an external replacement. To the best of my knowledge, this is the first study to examine the influence of negative media coverage on successor origin.

Results of H4 and H5: CEO Dismissal, CEO Successor Origin, and Change in Negative Media Coverage

To test H4 and H5, Table 3.7 presents models which examine the impact of CEO dismissal and external replacement on the change in *NEG_MEDIA*. This analysis is important for addressing endogeneity concerns. Since I have data on the exact date of the CEO turnover event, and monthly index values for data on negative media coverage, I am able to cleanly separate negative media coverage before and after the turnover event.[80] Changes to media coverage can therefore be attributed to the turnover event. Additionally, because *NEG_MEDIA* is an index variable, there is significant variation to examine this change, which has been a difficult task in previous media studies.

[80] The sample size is smaller for this analysis than for previous due to the loss of firm-year observations with turnover after 2014. These observations do not have complete data necessary to construct differenced variables. Specifically, I cannot construct one-year-ahead data from RepRisk and other databases.

[INSERT TABLE 3.7 HERE]

The dependent variable in this analysis is Δ*NEG_MEDIA*. For firm-year observations with CEO dismissal, this is measured as the index value twelve months after turnover less the maximum index value twelve months prior to turnover (i.e., the *NEG_MEDIA* value used in earlier analyses). For firm-year observations without a CEO dismissal, this is measured as the maximum index in *t*+1 less the maximum index in *t* (i.e., the *NEG_MEDIA* value used in earlier analyses).[81] All continuous control variables, with the exception of departing CEO age, are measured as the one-year change (year after turnover less year of turnover). Additionally, indicator variables for restatement and material weakness are measured as a one-year change to account for the impact of newly disclosed financial reporting issues on the change in negative media coverage.

Results in Column 1 of Table 3.7 show that *CEO_DISMISSAL* is inversely associated with Δ*NEG_MEDIA*. In other words, negative media coverage decreases following a CEO dismissal. This supports H4. However, it does not appear that CEO successor origin impacts this change. Specifically, *EXTERNAL_CEO* is not significant in Column 2. I note that the true impact of dismissal due to negative media coverage may be masked in these samples by firms that had low levels of coverage to begin with, and thus removed their CEO for other reasons. Therefore, the sample in Columns 3 and 4 is constrained to firms that had above median values of *NEG_MEDIA* pre-turnover, or in the fiscal year in which they did not have a turnover event. This allows a comparison of negative coverage declines amongst firms who had high levels before making the turnover

[81] Results are similar if Δ*NEG_MEDIA* is measured in several different ways (e.g., post index measured as the minimum or peak within several constrained time periods (e.g., six months after, 24 months after, FYE for non-turnover observations, etc.), percentage change, pre-index measured within several constrained time periods (e.g., six months, at the turnover date for turnover observations, etc.).

decision. Findings in these samples again support H4 and do not support H5.[82] This confirms theory that when facing negative media attention, boards that hold the CEO publicly accountable mitigate this coverage.

Combined, it appears that CEO dismissal is necessary for recovery when high reach media sources focus on ESG issues, but that the new CEO's origin does not matter for recovery. It is interesting that, anecdotally, the media pushes for external CEO replacements (e.g., Boston 2015; Harris 2014), but negative coverage persists regardless of the successor's origin. Therefore, boards who follow the conventional wisdom that an external replacement is needed in reputation-damaging situations may make suboptimal replacement decisions by anchoring on successor origin.

Additional Analyses

ESG-focused Institutional Ownership as an Additional Pressure

Prior literature has suggested that the investment community serves as an additional monitoring mechanism (e.g. Burns, Kedia, and Lipson 2010; Ramalingegowda and Yu 2012). Recently, investment management companies have differentiated themselves by offering funds that incorporate ESG criteria into portfolio formation and analysis. In fact, growth in ESG assets under management has outpaced growth in the general asset management base (GSIA 2014). It is interesting to examine whether additional external pressure, via inclusion in and thus monitoring by ESG-focused funds, makes boards more likely to react to negative coverage of ESG practices. Two popular ESG-focused funds, Vanguard FTSE Social Index Fund and iShares MSCI KLD Social ETF, list objectives to screen for "certain social, human rights, and environmental criteria" and "positive

[82] Coefficient comparisons for *CEO_DISMISSAL* between Columns 1 and 3 suggest that negative media coverage declines to a greater extent for firms that had high levels of coverage before the turnover decision.

environmental, social and governance characteristics," respectively. I obtain holdings data from Thomson Reuters and re-estimate results within a sample of firms that are held by the listed funds. Table 3.8 presents these results.

[INSERT TABLE 3.8 HERE]

In this isolated sample, I find all measures of ESG negative media coverage to be positively associated with CEO dismissal likelihood. Compared to findings in the full sample, boards of companies held by ESG-conscious funds are more likely to dismiss their CEO following coverage of environmental and social issues. This difference is statistically significant, as evidenced by significant coefficient comparisons between the two samples.[83] These results imply that corporate boards adhere to investor demands concerning the desired level of sensitivity to ESG issues. ESG-conscious institutional ownership appears to encourage boards to take all ESG issues, including previously undocumented environmental and social issues, seriously.

Board Characteristics as Moderating Variables

Prior literature has shown certain board characteristics to influence the likelihood of CEO dismissal (e.g., Fich and Shivdasani 2006). Decisions regarding executive turnover are directly controlled by the board, and therefore resource dedication to the board is likely to impact the association between negative media coverage and CEO dismissal likelihood. Therefore, I conduct analyses that include interactions between the measures of negative media coverage and certain board characteristics. Results of these analyses are presented in Table 3.9.

[83] I also compare this sample of companies held by ESG-conscious funds to a sample of companies not held by these funds. Consistent with the tabled results, I find that coefficients on *E_ISSUE* and *S_ISSUE* are significantly greater in the sample of companies held by ESG-conscious mutual funds.

[INSERT TABLE 3.9 HERE]

Table 3.9 Panel A examines the existence of a board-level sustainability committee as a moderating variable. The existence of these committees indicates board sensitivity to ESG issues, as they are a voluntary means to oversee the impact of ESG-related issues on firm performance (Burke, Hoitash, and Hoitash 2017). Boards that voluntarily dedicate resources to this oversight may be more likely to react to negative media coverage. In this analysis, *COMMITTEE* is an indicator variable equal to one if the firm-year observation has a board-level committee with sustainability responsibilities explicitly listed in their proxy filing, and zero otherwise.[84] I find significant and positive interactions between this variable and *E_ISSUE* and *S_ISSUE* (Columns 2 and 3, respectively). I do not find a significant interaction between *COMMITTEE* and *G_ISSUE*.[85] This suggests that boards with sustainability committees, which are a signal of sensitivity to ESG issues, are more likely to dismiss their CEO following negative coverage of environment and social practices.

Table 3.9 Panel B examines board size as a moderating variable to the association between negative media coverage and CEO dismissal likelihood. An extensive literature debates the impact of board size on a board's monitoring quality (e.g., Coles, Daniel, and Naveen 2008; Cheng 2008; Yermack 1996) and largely finds that smaller boards are better monitors. Consistent with this, I expect that larger boards will be less likely to hold a CEO publicly accountable for negative media coverage. Column 4 shows that *G_ISSUE* *

[84] To identify these committees, I hand collect committee responsibilities from the annual proxy filings of companies that have a board-level committee with a name that suggests a sustainability focus. The sample for this analysis is limited to 2007-2013 because the variable requires extensive hand collection.

[85] As defined in Burke et al. (2017), the committee variable captures committees that oversee responsibilities related to the community, employees, the environment, consumers, and suppliers. Thus, it is not surprising that I do not find a significant interaction with *G_ISSUE* since responsibilities for the oversight of these issues rests outside of sustainability committees, likely with the full board.

*BOARD_SIZ*E is negative and significant, which confirms the expectation that larger boards are less likely to dismiss their CEO when governance issues are subject to negative media coverage. I do not find that board size is a significant moderating factor to the associations between other measures of negative media coverage and CEO dismissal likelihood.

Table 3.9 Panel C examines board busyness as a moderating variable. Fich and Shivdasani (2006) find that busy boards are less likely to remove a CEO for poor performance. Similarly, I expect that busy boards are less likely to hold a CEO publicly accountable for negative media coverage. *BOARD_BUSY* is an indicator variable equal to one if more than 50 percent of directors are busy, and zero otherwise. A busy director is defined as an independent director that serves on three or more boards (Fich and Shivdasani 2006). Consistent with this expectation and with board size results, I find that busy boards are less likely to remove their CEO following coverage of governance issues (i.e., *G_ISSUE * BOARD_BUSY* is negative and significant in Column 4), but do not find that board busyness influences the association for other measures of negative media coverage.

In sum, findings suggest that boards that have a formal committee to oversee sustainability issues are more likely to dismiss their CEO when facing negative coverage of environmental and social issues, suggesting that monitoring ESG risks is more important to these companies. Conversely, larger and busier boards are less likely to hold CEOs publicly accountable for negative media coverage of governance issues. This is consistent with these characteristics harming the monitoring ability of the board and extends literature that examines board monitoring quality.

Financial Performance as a Moderating Variable

An extensive literature finds that executives are held accountable for poor performance (e.g., Coughlan and Schmidt 1985; Murphy and Zimmerman 1993; Weisbach 1988). Relatedly, if firms are performing well financially, it is possible that negative media coverage of ESG issues is seen as less important. For instance, a board may not punish a CEO who oversees a firm with high stock returns that has a few pollution or human rights issues. Somewhat surprisingly, in untabulated results I do not find a significant interaction between two measures of financial performance, stock return and return on assets, and all four measures of negative media coverage. This suggests that CEOs are held accountable for ESG issues regardless of financial performance. While I do not claim that the covered ESG issues are independent from financial issues, this result alleviates the concern that results are driven solely by financial performance consequences of the issues. It appears that turnover occurs before these consequences, if any, are realized. I leave the question of whether these issues cause financial consequences down the line open for future research.

V. SUMMARY AND CONCLUSIONS

Recent anecdotes suggest that negative media coverage of ESG issues can prompt CEO turnover, yet this has not been empirically examined. It is not clear whether, on average, media coverage of ESG issues are important to board deliberations, and thus whether they impact turnover decisions. To address this gap in the literature, I investigate (a) negative media coverage of ESG practices as a determinant to CEO dismissal, (b) the impact of this coverage on CEO replacement decisions, and (c) subsequent declines in coverage attributed to the CEO turnover event.

Unique data on this media coverage, made available by RepRisk, affords this research opportunity. The limited literature that has examined negative media coverage has

manually collected news stories. RepRisk collects media coverage from a comprehensive range of sources, which vary in their prominence, and quantifies ESG-related negative media coverage. This quantification is based on the existence of news, the severity of underlying issues, and the reach of the media source that issues are identified in. Using this data, I examine the prediction that the media, via its influence on public opinion, can motivate directors to remove a CEO.

Consistent with my predictions, I find that CEOs are held accountable for negative media coverage of ESG issues. I generally find that severe issues that are highly publicized drive this finding. Interestingly, for coverage of governance issues, the likelihood of CEO dismissal is impacted regardless of the issue's severity. This, combined with several additional analyses, suggests that the coverage of an issue is incremental to the impact of the underlying issue in influencing CEO dismissal likelihood. These results confirm the monitoring role of the media by illustrating that highly publicized ESG issues garner boardroom attention and, on average, result in CEO dismissal. For firms that replace their CEO, I further find that coverage of governance issues is positively associated with the likelihood of an external CEO successor. Importantly, I also find that CEO dismissal is effective at alleviating negative media coverage, but that this recovery is not contingent on the successor's origin (i.e., internal or external).

Overall, the findings of this study contribute to research and practice. Recent media frenzies surrounding reputation-damaging incidents present a timely environment in which to examine executive turnover, replacement, and subsequent improvement in media coverage of ESG practices. Results can potentially inform boards that are faced with a CEO turnover replacement decision following negative media attention. Specifically, findings

suggest that CEO dismissal may be necessary following highly publicized and severe ESG issues, but that the chosen successor's origin does not impact future negative media coverage.

Figure 1.1 Graph of committee focus over time

The above graph displays the focus over time of the 1,243 sustainability committees in our unbalanced panel dataset. Community focused committees are those that focus on community and/or human rights related issues; employee focused committees are those that focus on employee and diversity related issues; environment committees are those that focus on environment related issues; lastly, consumer and supplier focused committees are those that focus on product related issues.

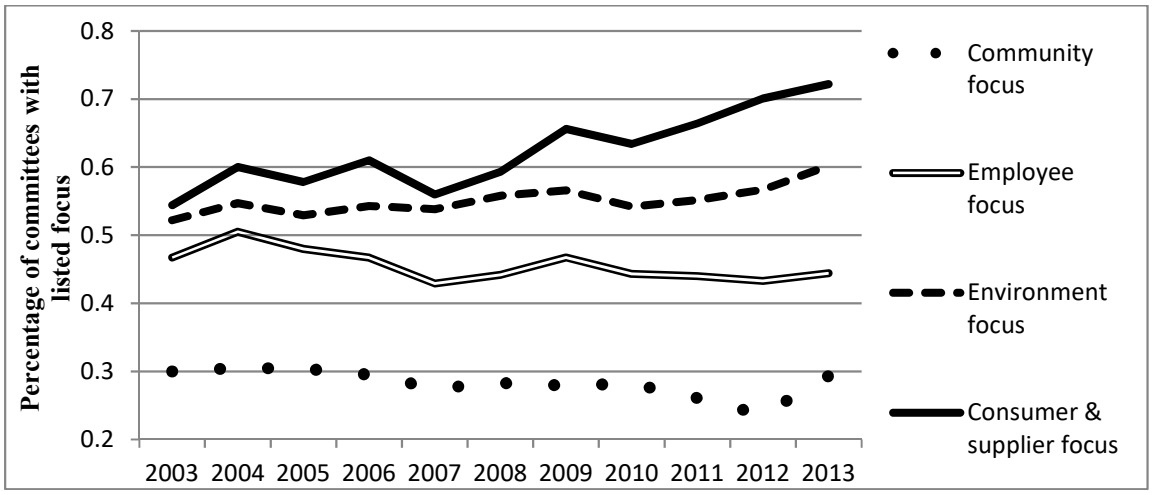
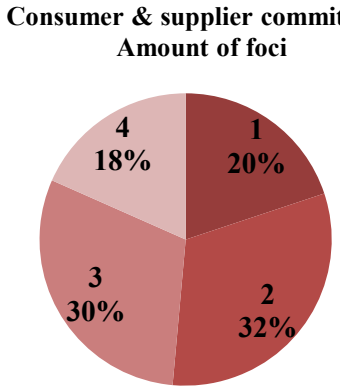
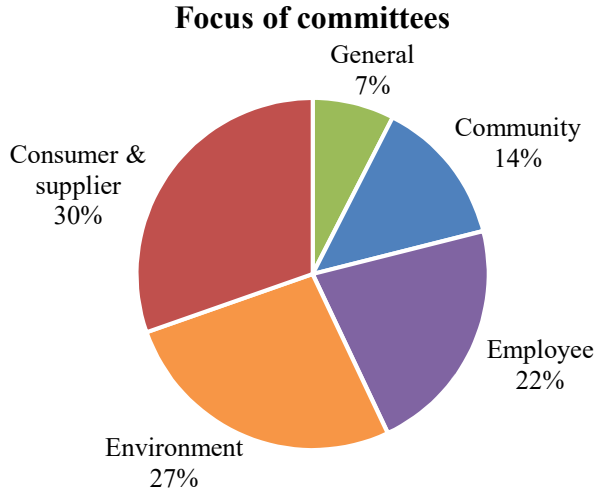
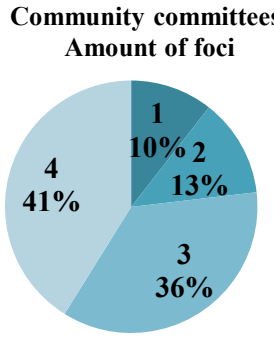
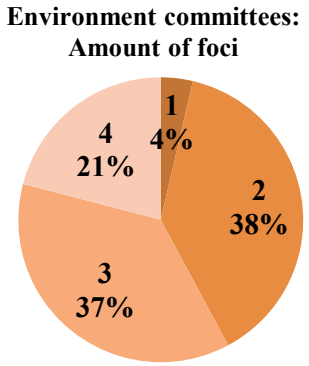


Figure 1.2 Charts of committee foci









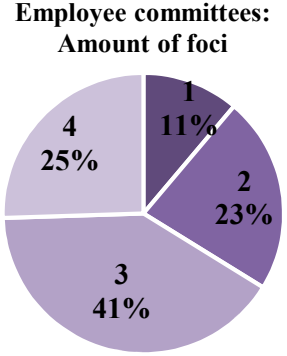
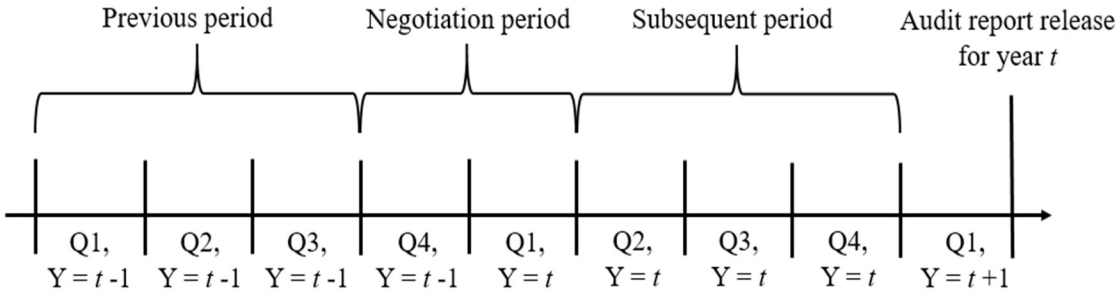


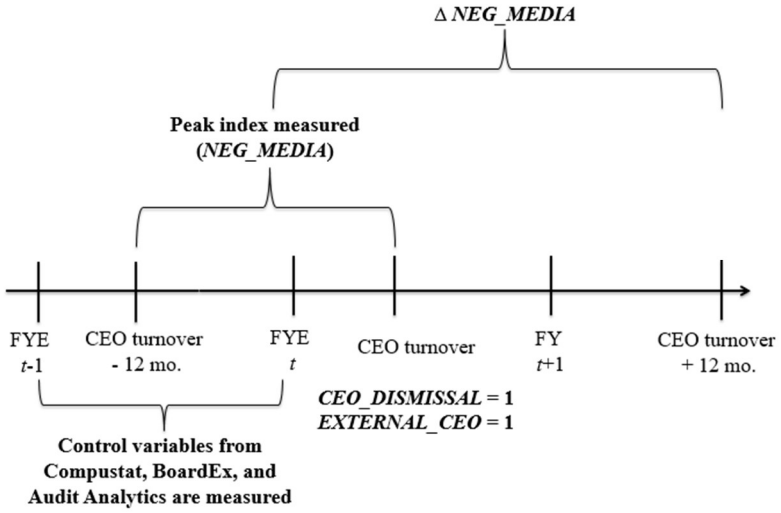
Figure 2.1 Timing of the audit process



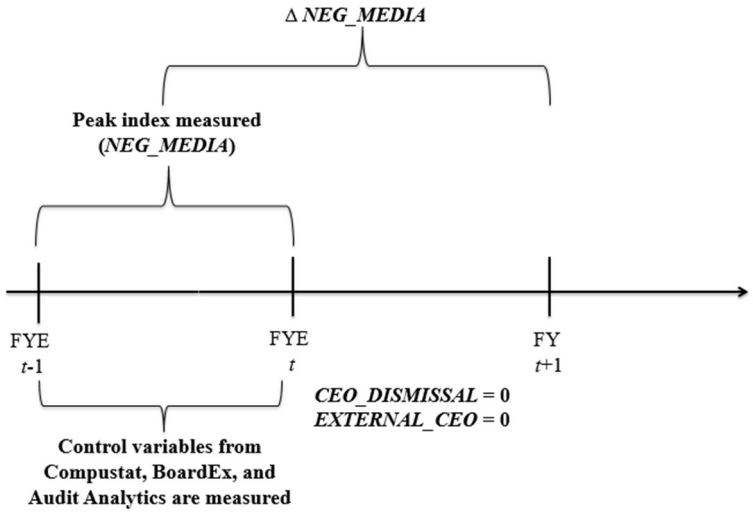
This figure is adapted from Hackenbrack et al. (2014), who interview Big 4 partners to develop a timeline for auditor-client negotiations and find that negotiation concludes with engagement letter signing at the end of the first quarter of the year under audit. Using RepRisk's monthly data, we are able to measure negative media coverage in periods previous, during, and subsequent to the negotiation period. Q1, Q2, and Q3 of year *t*-1 ("previous period") have the potential to impact the year *t* audit engagement and associated fees. Q4 of year t-1 and Q1 of year *t* ("negotiation period") represent the period in which coverage is most salient to the negotiation of the year *t* audit fee. Our primary measure (*NEG_MEDIA*) is taken within this period. Q2, Q3, and Q4 of year *t* ("subsequent period") capture the period in which firm activity will be reported in the year *t* audit report. Lastly, the audit report for year *t* is released shortly after the end of Q1 in year *t*+1.

Figure 3.1 Variable measurement example

Treated observation (*CEO_DISMISSAL* = 1)

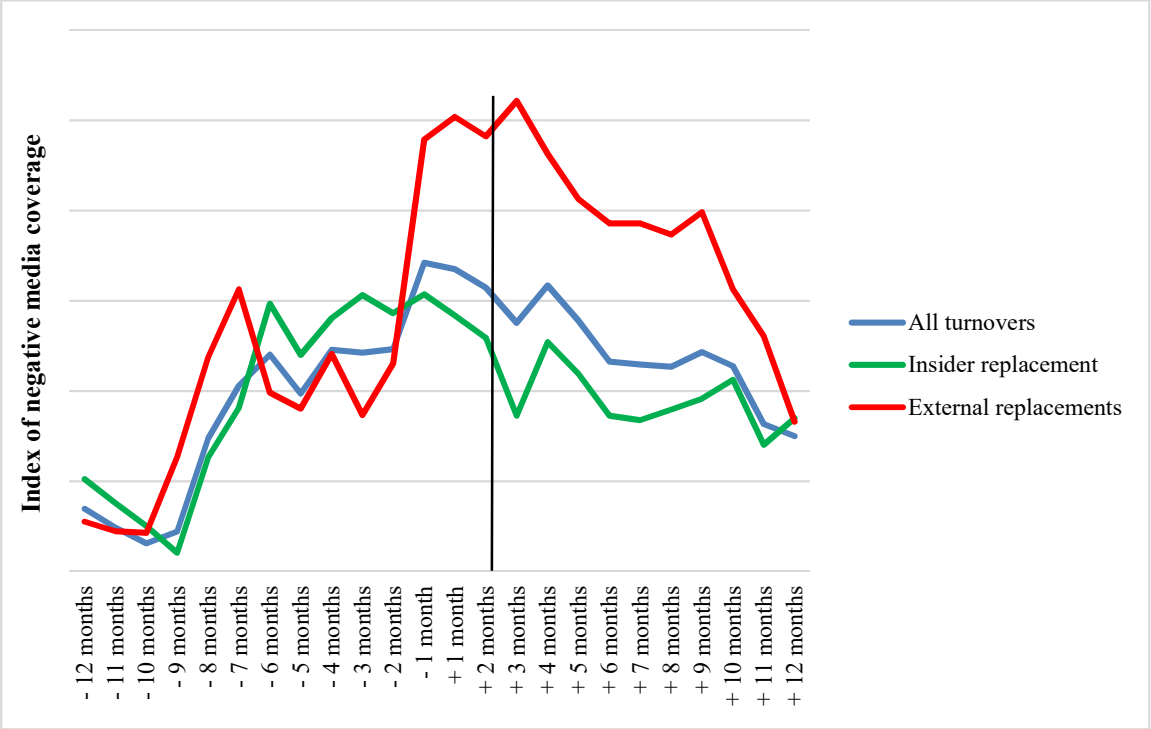


Untreated observations (*CEO_DISMISSAL* = 0)



This figure illustrates variable timing used in main analyses. Specifically, the first timeline illustrates variable timing for a treated (i.e., has a CEO dismissal) observation, and the second illustrates variable timing for a non-treated (i.e., does not have a CEO dismissal) observation during year *t*. As described throughout the text and in Appendix F, *NEG_MEDIA* is the dismissal negative media coverage of ESG practices within the twelve months prior to the CEO turnover date for firm-year observations with a CEO turnover, and within the fiscal year for firm-year observations without a CEO dismissal. These ranges are noted on the figures. For the treated observation, *CEO_DISMISSAL* and *EXTERNAL_CEO* are both equal to one. The fiscal year assigned to this observation, along with the timing of all variables that are only provided on an annual basis (e.g., Compustat, Audit Analytics, BoardEx), is that with the closest year-end to the turnover date. The control group in this fiscal year is any firm where *CEO_DISMISSAL* is equal to zero. All variables for these untreated observations are measured during year *t*. This includes *NEG_MEDIA*, which is equal to the maximum negative media coverage of ESG practices during year *t*. Finally, Δ*NEG_MEDIA* is measured as the index value twelve months after turnover less the maximum index value twelve months prior to turnover (i.e., *NEG_MEDIA*) for firms with dismissal. For firms without dismissal, Δ*NEG_MEDIA* is measured as the maximum index value in year *t*+1 less the maximum index in year *t*.

Figure 3.2 Graph of negative media coverage surrounding CEO dismissal



This graph plots mean monthly values of the index of negative media coverage of ESG practices, as provided by RepRisk, within firm-year observations that have a CEO dismissal. The blue line represents mean monthly values for all dismissals, the green internal replacements, and the red external replacements. The X axis displays the distance to the turnover event (marked by the vertical black line).

Table 1.1 Sample information

Description	Sample size
All firm-year observations from 2003—2013 with available MSCI ESG STATS data	31,167
Less: missing Compustat control variable data	(5,531)
Less: missing BoardEx control variable data	(14,178)
Total firm-year observations available from 2003—2013	*11,458*

Table 1.2 Summary statistics

Panel A and B display summary statistics of dependent and control variables within the full sample of 11,458 firm-year observations. Variables are defined in Appendix A. Panel C displays simple correlations for key variables employed in our analysis. Correlations that are significant at a level below 10 percent (two-tailed) are in bold.

Panel A: Summary statistics of dependent variables

	Mean	Median	Std. Dev.	Min	Max
CSP score	0.24	0.00	2.73	-9.00	18.00
CSP strengths	1.83	1.00	2.74	0.00	21.00
CSP concerns	1.59	1.00	1.70	0.00	14.00
Community strengths	0.21	0.00	0.59	0.00	7.00
Community concerns	0.14	0.00	0.42	0.00	5.00
Employee strengths	1.16	0.00	1.70	0.00	12.00
Employee concerns	0.92	1.00	0.91	0.00	6.00
Environment strengths	0.36	0.00	0.83	0.00	5.00
Environment concerns	0.27	0.00	0.69	0.00	5.00
Consumer and supplier strengths	0.10	0.00	0.33	0.00	3.00
Consumer and supplier concerns	0.26	0.00	0.60	0.00	4.00

Panel B: Summary statistics of control variables

	Mean	Median	Std. Dev.	Min	Max
Board size (log)	2.17	2.20	0.25	0.00	3.53
Board size	9.03	9.00	2.22	1.00	34.00
Independence	0.76	0.78	0.13	0.10	1.00
Tenure	8.74	8.20	3.85	0.00	30.00
Busy board	0.16	0.00	0.37	0.00	1.00
Size	7.65	7.51	1.47	3.96	12.54
Total assets	7,585.99	1,854.77	19,782.07	52.24	27,7787.00
Quick	2.41	1.92	1.94	0.20	35.70
ROA	0.05	0.06	0.10	-1.77	0.78
Leverage	0.18	0.16	0.16	0.00	2.88
R&D investment	0.04	0	0.11	0	3.94

Panel C: Correlation matrix of key variables

	1	2	3	4	5	6
1. CSP score						
2. CSP strengths	**0.81**					
3. CSP concerns	**-0.31**	**0.31**				
4. Committee	**0.11**	**0.29**	**0.30**			
5. Board size	**0.23**	**0.37**	**0.23**	**0.26**		
6. Independence	**0.13**	**0.20**	**0.12**	**0.16**	**0.17**	
7. Size	**0.31**	**0.60**	**0.47**	**0.32**	**0.56**	**0.22**

Table 1.2 (continued)

Panel D: Committee focus detail

Committee focus	Count	Percentage
Community	37	2.98
Employee	63	5.07
Environment	25	2.01
Consumer/supplier	156	12.55
Community & employee	24	1.93
Community & environment	9	0.72
Community & consumer/supplier	11	0.88
Community, employee & environment	45	3.62
Community, employee & consumer/supplier	28	2.25
Community, environment & consumer/supplier	52	4.18
Community, employee, environment & consumer/supplier	144	11.58
Employee & environment	62	4.99
Employee & consumer/supplier	42	3.38
Employee, environment & consumer/supplier	157	12.63
Environment & consumer/supplier	194	15.61
General	194	15.61

Table 1.3 The impact of sustainability committees on CSP: OLS results using aggregate measures

	CSP score		CSP strengths		CSP concerns	
	Coefficient	SE	Coefficient	SE	Coefficient	SE
Independent variables						
Committee	0.30	(0.23)	1.01***	(0.19)	0.70***	(0.14)
Board size	1.02***	(0.19)	0.51***	(0.17)	-0.51***	(0.11)
Independence	0.81**	(0.33)	0.88***	(0.28)	0.08	(0.21)
Tenure	-0.01	(0.01)	-0.02*	(0.01)	-0.00	(0.01)
Busy board	-0.13	(0.12)	0.12	(0.10)	0.24***	(0.07)
Size	0.64***	(0.07)	1.12***	(0.06)	0.48***	(0.03)
Quick	-0.01	(0.02)	0.02	(0.02)	0.03***	(0.01)
ROA	1.44***	(0.36)	0.95***	(0.31)	-0.48**	(0.19)
Leverage	-1.51***	(0.30)	-1.96***	(0.28)	-0.46***	(0.15)
R&D investment	2.04***	(0.85)	1.11*	(0.66)	-0.94***	(0.26)
Industry fixed effects	Yes		Yes		Yes	
Year fixed effects	Yes		Yes		Yes	
Constant	-10.44***	(1.04)	-7.72***	(0.62)	2.72**	(1.14)
Model statistics						
N (sample size)	11,458		11,458		11,458	
Adjusted R^2	0.24		0.45		0.38	

Variables are defined in Appendix A. Standard errors are clustered by firm and reported in parentheses. ***, **, and * indicate significance levels below 0.01, 0.05, and 0.10, respectively (two-tailed).

To formally test increase in explanatory power when separating the dependent variable into total strengths and total concerns, we use the Vuong test statistic to show a significance increase in R^2 from Model A to Models B and C:

CSP score R^2	CSP strengths R^2	CSP concerns R^2	Vuong Z-statistic
0.24	0.45		-22.80***
0.24		0.38	-47.46***

Table 1.4 The impact of sustainability committees on CSP: OLS results using disaggregated measures

Panel A: CSP strengths	Community strengths		Employee strengths		Environment strengths		Consumer/supplier strengths	
	Coeff.	SE	Coeff.	SE	Coeff.	SE	Coeff.	SE
Independent variables								
No community focus	0.08*	(0.05)						
Community focus	0.35***	(0.11)						
No employee focus			0.36**	(0.14)				
Employee focus			0.80***	(0.17)				
No environment focus					0.03	(0.06)		
Environment focus					0.41***	(0.08)		
No consumer/supplier focus							0.08**	(0.04)
Consumer/supplier focus							0.04	(0.03)
Controls from Table 1.3	Yes		Yes		Yes		Yes	
Constant	-1.41***	(0.15)	-3.80***	(0.51)	-2.05***	(0.18)	-0.54***	(0.07)
Model statistics								
N (sample size)	11,458		11,458		11,458		11,458	
Adjusted R^2	0.27		0.39		0.35		0.12	
Results of F-tests for significant difference in the coefficients of these mutually exclusive indicator variables are as follows:								
No community focus vs. community focus					5.90***			
No employee focus vs. employee focus					5.17***			
No environment focus vs. environment focus					14.73***			
No consumer/supplier focus vs. consumer/supplier focus					0.88			

Panel B: CSP concerns	Community concerns		Employee concerns		Environment concerns		Consumer/supplier concerns	
	Coeff.	SE	Coeff.	SE	Coeff.	SE	Coeff.	SE
Independent variables								
No community focus	0.10**	(0.05)						
Community focus	0.11	(0.07)						
No employee focus			0.04	(0.07)				
Employee focus			0.10	(0.07)				
No environment focus					0.14*	(0.08)		
Environment focus					0.45***	(0.10)		
No consumer/supplier focus							0.29***	(0.09)
Consumer/supplier focus							0.19***	(0.06)
Controls from Table 1.3	Yes		Yes		Yes		Yes	
Constant	0.28	(0.34)	0.83	(0.51)	1.19	(0.72)	0.36	(0.52)
Model statistics								
N (sample size)	11,458		11,458		11,458		11,458	
Adjusted R^2	0.25		0.18		0.41		0.33	
Results of F-tests for significant difference in the coefficients of these mutually exclusive indicator variables are as follows:								
No community focus vs. community focus					0.00			
No employee focus vs. employee focus					0.47			
No environment focus vs. environment focus					5.91***			
No consumer/supplier focus vs. consumer/supplier focus					0.74			

Variables are defined in Appendix A. Standard errors are clustered by firm and reported in parentheses. ***, **, and * indicate significance levels below 0.01, 0.05, and 0.10, respectively (two-tailed).

Table 1.5 Further committee characteristics: Summary statistics and univariate comparisons of effectiveness

Panel A displays summary statistics of committee characteristics within the full available sample and separately within samples of community, employee, environment, and consumer/supplier focused committees. Panel B displays univariate comparisons of these characteristics within the full committee and each group of focused committee samples.

Panel A: Summary statistics of committee characteristics

	N	Minimum	25th percentile	Mean	Median	75th percentile	Maximum
All committees							
Committee size	1196	1.000	4.000	4.539	4.000	5.000	16.000
Fully independent	1196	0.000	1.000	0.753	1.000	1.000	1.000
Meeting frequency	1196	0.000	2.000	3.896	4.000	5.000	12.000
Community focused							
Committee size	331	1.000	4.000	4.498	4.000	5.000	9.000
Fully independent	331	0.000	1.000	0.752	1.000	1.000	1.000
Meeting frequency	331	0.000	2.000	3.628	3.000	5.000	11.000
Employee focused							
Committee size	539	1.000	4.000	4.412	4.000	5.000	9.000
Fully independent	539	0.000	1.000	0.787	1.000	1.000	1.000
Meeting frequency	539	0.000	2.000	3.571	4.000	5.000	11.000
Environment focused							
Committee size	667	1.000	4.000	4.675	4.000	5.000	13.000
Fully independent	667	0.000	1.000	1.000	1.000	1.000	1.000
Meeting frequency	667	0.000	2.000	3.550	4.000	5.000	11.000
Consumer/supplier focused							
Committee size	764	1.000	4.000	4.723	4.000	5.000	16.000
Fully independent	764	0.000	0.000	0.733	1.000	1.000	1.000
Meeting frequency	764	0.000	2.000	3.728	4.000	5.000	12.000

Panel B: Univariate comparisons: committee characteristics by effectiveness

	"Ineffective" committees		"Effective" committees			
	Count	Mean	Count	Mean	t-stat for difference	p-value
All committees						
Committee size	748	4.394	448	4.781	-4.246	0.000
Fully independent	748	0.730	448	0.792	-2.430	0.015
Meetings	748	3.743	448	4.152	-3.125	0.002
Community focus						
Committee size	165	4.364	166	4.633	-2.244	0.025
Fully independent	165	0.679	166	0.825	-3.123	0.002
Meetings	165	3.364	166	3.892	-3.131	0.002
Employee focus						
Committee size	259	4.193	280	4.614	-4.372	0.000
Fully independent	259	0.772	280	0.800	-0.786	0.432
Meetings	259	3.425	280	3.707	-2.078	0.038
Environment focus						
Committee size	464	4.651	203	4.729	-0.616	0.538
Fully independent	464	0.746	203	0.798	-1.460	0.145
Meetings	464	3.461	203	3.754	-2.292	0.022
Consumer/supplier focus						
Committee size	636	4.701	128	4.828	-0.794	0.428
Fully independent	636	0.717	128	0.812	-2.233	0.026
Meetings	636	3.692	128	3.906	-1.315	0.189

Table 1.6 Univariate comparisons of committee focus, by sensitive industry

	Not in sensitive industry		In sensitive industry		
	Count	Mean	Count	Mean	t-stat for difference
Full sample comparison					
Community focus	10,510	0.03	948	0.08	-8.51***
Employee focus	10,259	0.05	1,199	0.09	-6.76***
Environment focus	7,941	0.02	3,517	0.15	-28.48***
Consumer/supplier focus	9,366	0.06	2,092	0.09	-4.49***
Committee sample comparison					
Community focus	1,068	0.26	175	0.41	-4.15***
Employee focus	1,066	0.43	177	0.61	-4.36***
Environment focus	486	0.32	757	0.71	-14.53***
Consumer/supplier focus	922	0.64	321	0.59	1.67*

p-values: * $p < 0.10$. ** $p < 0.05$. *** $p < 0.01$

Table 1.6 (continued)

Sensitive industry definitions (by 2 digit SIC code)

Community sensitive industries:	01, 10, 12, 16, 21, 29, 31, 39, 40, 48, 53, 54, 61, 65, 70, 99
Employee sensitive industries:	01, 10, 20, 21, 29, 40, 45, 48, 52, 53, 54, 61, 65, 70, 75, 99
Environment sensitive industries:	01, 10, 12, 13, 20, 22, 24, 25, 26, 28, 29, 33, 37, 40, 49, 99
Consumer/supplier sensitive industries:	01, 02, 20, 21, 28, 40, 45, 48, 53, 54, 61, 62, 63, 64, 99

Division	**2-digit SIC code**	**Sensitive industries**
Agriculture, forestry, and fishing	01-09	01 (agriculture products – crops); 02 (agricultural production – livestock)
Mining	10-14	10 (metal, mining); 12 (coal mining); 13 (oil and gas extraction)
Construction	15-17	16 (heavy construction, except building)
Manufacturing	20-39	20 (food and kindred products); 21 (tobacco products); 22 (textile mill products); 24 (lumber and wood products); 25 (furniture and fixtures); 26 (paper and allied products); 28 (chemical and allied products); 29 (petroleum & coal products); 31 (leather & leather products); 33 (primary metal industries); 37 (transportation equipment); 39 (miscellaneous manufacturing industries)
Transportation and public utilities	40-49	40 (railroad transportation); 45 (transportation by air); 48 (communications); 49 (electric, gas, and sanitary services)
Retail trade	52-59	52 (building materials and gardening supplies); 53 (general merchandise stores); 54 (food stores)
Finance, insurance, and real estate	60-67	61 (nondepository institutions); 62 (security and commodity brokers); 63 (insurance carriers); 64 (insurance agents, brokers and service); 65 (real estate)
Services	70-89	70 (hotels and other lodging places); 75 (auto repair, services, and parking),
Non-classifiable establishments	99	99 (non-classifiable establishments)

Table 1.7 Sensitive industry analysis, the impact of sustainability committees on CSP: OLS using disaggregated measures in sensitive industries

Panel A: CSP strengths	Community strengths		Employee strengths		Environment strengths		Consumer/supplier strengths	
	Coeff.	SE	Coeff.	SE	Coeff.	SE	Coeff.	SE
Independent variables								
Community focus	1.02***	(0.28)						
Employee focus			1.22***	(0.29)				
Environment focus					0.37***	(0.09)		
Consumer/supplier focus							-0.00	(0.07)
Controls from Table 1.3	Yes		Yes		Yes		Yes	
Constant	-2.36***	(0.54)	-6.95***	(1.38)	-3.15***	(0.34)	-0.62***	(0.15)
Model statistics								
N (sample size)	948		1,199		3,517		2,092	
Adjusted R^2	0.37		0.47		0.40		0.19	

Panel B: CSP concerns	Community concerns		Employee concerns		Environment concerns		Consumer/supplier concerns	
	Coeff.	SE	Coeff.	SE	Coeff.	SE	Coeff.	SE
Independent variables								
Community focus	0.23	(0.16)						
Employee focus			-0.03	(0.18)				
Environment focus					0.39***	(0.12)		
Consumer/supplier focus							-0.04	(0.15)
Controls from Table 1.3	Yes		Yes		Yes		Yes	
Constant	-0.80	(0.50)	-0.22	(1.11)	-0.35	(0.66)	-0.75	(0.56)
Model statistics								
N (sample size)	948		1,199		3,517		2,092	
Adjusted R^2	0.43		0.31		0.41		0.41	

Variables are defined in Appendix A. Standard errors are clustered by firm and reported in parentheses. ***, **, and * indicate significance levels below 0.01, 0.05, and 0.10, respectively (two-tailed).

Table 2.1 Sample derivation

Steps	**Observations**
Sample of 2007-2014 fiscal year companies covered in RepRisk	15,160
Merge with Compustat (observations with non-missing total assets or sales)	9,348
Merge with Audit Analytics (observations with non-missing audit fees)	9,005
Final sample (after deleting firms without necessary control variable data)	**7,754**

Table 2.2 Descriptive statistics

Panel A: Summary statistics

N = 7,754	Mean	Median	Standard deviation	25th percentile	75th percentile
Risk measures					
NEG_MEDIA (unadjusted)	10.171	0.000	13.857	0.000	22.000
NEG_MEDIA	1.032	0.000	1.678	0.000	1.805
E_ISSUE	0.126	0.000	0.332	0.000	0.000
S_ISSUE	0.160	0.000	0.366	0.000	0.000
G_ISSUE	0.107	0.000	0.309	0.000	0.000
Auditor response					
AUDITORCHANGE	0.029	0.000	0.168	0.000	0.000
RESIGN	0.004	0.000	0.062	0.000	0.000
Audit Fees ($)	$3,837,775	$2,014,295	$5,201,309	$1,033,790	$4,500,000
LOGAUDITFEES	14.567	14.516	1.091	13.849	15.320
Control variables					
LNASSETS	7.824	7.887	1.768	6.703	8.999
ROA	0.029	0.047	0.126	0.015	0.084
LEVERAGE	0.227	0.204	0.192	0.076	0.324
SALESGROWTH	0.172	0.055	3.696	-0.020	0.147
ZSCORE	3.917	4.000	2.070	2.000	6.000
MA	0.252	0.000	0.434	0.000	1.000
FOREIGN	0.128	0.000	0.334	0.000	0.000
P_SCORE	-1.812	-1.763	0.119	-1.770	-1.758
RESTATEMENT	0.072	0.000	0.259	0.000	0.000
GC	0.013	0.000	0.113	0.000	0.000
INDUSTRYEXP	0.098	0.000	0.298	0.000	0.000
FYE_DEC	0.750	1.000	0.433	0.000	1.000
SEGMENTS	1.778	1.000	1.030	1.000	2.000
MW	0.058	0.000	0.233	0.000	0.000
Supplemental variables					
NEGMEDIA_PEAK_PRIOR	0.031	0.000	0.174	0.000	0.000
NEGMEDIA_PEAK_NEGOT	0.047	0.000	0.211	0.000	0.000
NEGMEDIA_PEAK_SUBSEQUENT	0.251	0.000	0.434	0.000	1.000
BENFORD_SCORE	0.074	0.068	0.032	0.051	0.091
BENFORD_FAIL	0.158	0.000	0.365	0.000	0.000
ABFEE	0.000	0.009	0.438	-0.287	0.285
NEW_GC	0.003	0.000	0.057	0.000	0.000
MISSTATEMENT	0.129	0.000	0.336	0.000	0.000
DACC	0.052	0.036	0.062	0.017	0.068
TACC	0.048	0.031	0.061	0.014	0.061
DELAY	58.371	58.000	10.598	53.000	60.000
DELAY_ADJ	-5.465	-4.000	8.571	-9.000	-1.000
OANCF	1,108	249	3,474	66	796
BIG4	0.888	1.000	0.315	1.000	1.000
STDOPCASH_5YR	0.047	0.033	0.057	0.019	0.056
STDSALES_5YR	0.136	0.091	0.151	0.050	0.167
FIRM_AGE	28.948	22.000	18.336	14.000	46.000
LITRISK	0.045	0.000	0.207	0.000	0.000
DISTRESSED	0.215	0.000	0.411	0.000	0.000
LOWHIGH_SUM	0.058	0.000	0.392	0.000	0.000

Table 2.2 (continued)

Panel B: Correlation matrix

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
(1) *NEG_MEDIA*	1								
(2) *E_ISSUE*	0.491***	1							
(3) *S_ISSUE*	0.541***	0.648***	1						
(4) *G_ISSUE*	0.407***	0.351***	0.373***	1					
(5) AUDITORCHANGE	-0.012	-0.026*	-0.030**	-0.013	1				
(6) *LOGAUDITFEES*	0.391***	0.324***	0.353***	0.329***	-0.104***	1			
(7) *GC*	-0.024*	-0.023*	-0.022	-0.028*	0.0413***	-0.135***	1		
(8) *MISSTATEMENT*	-0.035**	-0.039***	-0.021	-0.014	0.025*	-0.034**	0.014	1	
(9) *MW*	-0.052***	-0.039***	-0.052***	-0.017	0.108***	-0.088***	0.104***	0.234***	1
(10) *DACC*	-0.092***	-0.098***	-0.088***	-0.028*	0.059***	-0.211***	0.193***	0.028*	0.069***

* $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Table 2.3 Negative media coverage and ESG issue descriptive by industry

	Sample distribution		*NEG_MEDIA (unadj)*	*E_ISSUE*		*S_ISSUE*		*G_ISSUE*	
	N	% of sample	Mean	N	% of industry	N	% of industry	N	% of industry
1: Consumer nondurables	630	8.12	14.067	98	15.56	162	25.71	112	17.78
2: Consumer durables	196	2.53	7.056	8	4.08	15	7.65	18	9.18
3: Manufacturing	949	12.24	9.609	97	10.22	149	15.7	86	9.06
4: Oil, gas and coal extraction and product	628	8.1	12.105	164	26.11	156	24.84	75	11.94
5: Chemicals and allied products	390	5.03	12.328	86	22.05	69	17.69	43	11.03
6: Business equipment	1,012	13.05	9.06	81	8	149	14.72	115	11.36
7: Telephone and television transmission	182	2.35	11.148	13	7.14	36	19.78	28	15.38
8: Utilities	546	7.04	13.923	172	31.5	152	27.84	37	6.78
9: Wholesale, retail and some services	1,089	14.04	9.571	95	8.72	131	12.03	91	8.36
10: Healthcare, medical equipment, and drug	748	9.65	7.735	26	3.48	40	5.35	94	12.57
11: Finance	381	4.91	7.029	16	4.2	32	8.4	34	8.92
12: Other	1,003	12.94	9.377	119	11.86	146	14.55	95	9.47

Table 2.4 Client negative media coverage and auditor changes

	Predicted sign	(1) *AUDITOR CHANGE*	(2) *AUDITOR CHANGE*	(3) *AUDITOR CHANGE*	(4) *AUDITOR CHANGE*
NEG_MEDIA	+	0.085**			
		(1.96)			
E_ISSUE	+		-0.023		
			(-0.08)		
S_ISSUE	+			0.079	
				(0.29)	
G_ISSUE	+				0.482**
					(1.70)
LNASSETS	+	0.114	0.143*	0.139*	0.131*
		(1.17)	(1.49)	(1.44)	(1.37)
ROA	-	-1.291***	-1.318***	-1.315***	-1.276***
		(-2.19)	(-2.23)	(-2.23)	(-2.15)
LEVERAGE	+	0.100	0.059	0.063	0.083
		(0.26)	(0.15)	(0.16)	(0.21)
SALESGROWTH	+	0.012***	0.012***	0.012***	0.012***
		(2.20)	(2.19)	(2.19)	(2.19)
ZSCORE	+	0.029	0.030	0.030	0.030
		(0.61)	(0.63)	(0.63)	(0.65)
MA	+	0.032	0.013	0.017	0.015
		(0.17)	(0.07)	(0.09)	(0.08)
FOREIGN	+	0.409**	0.412**	0.411**	0.415***
		(1.95)	(1.96)	(1.95)	(1.98)
P_SCORE	+	-0.801	-0.800	-0.803	-0.806
		(-1.31)	(-1.29)	(-1.30)	(-1.31)
RESTATEMENT	+	0.786***	0.770***	0.772***	0.769***
		(3.83)	(3.75)	(3.76)	(3.75)
GC	+	-0.456	-0.417	-0.423	-0.442
		(-1.20)	(-1.12)	(-1.13)	(-1.17)
LOGAUDITFEES	-	-0.737***	-0.725***	-0.728***	-0.745***
		(-4.73)	(-4.66)	(-4.67)	(-4.78)
INDUSTRYEXP	-	-0.119	-0.124	-0.126	-0.106
		(-0.37)	(-0.39)	(-0.39)	(-0.33)
Industry and year fixed effects		Included	Included	Included	Included
Constant		5.361**	5.237**	5.271**	5.475**
		(2.13)	(2.05)	(2.06)	(2.18)
Observations		7,245	7,245	7,245	7,245
Pseudo R^2		0.105	0.103	0.103	0.104

This table reports results of logit regressions estimating the association of client negative media coverage with the likelihood of auditor change. The test variables in Columns (1)-(4) are *NEG_MEDIA*, *E_ISSUE, S_ISSUE,* and *G_ISSUE*, respectively. *NEG_MEDIA* is the maximum client negative media coverage of ESG practices during the audit negotiation period (fourth quarter of *t*-1 and first quarter of *t*), adjusted by the negotiation period mean. *E_ISSUE, S_ISSUE,* and *G_ISSUE* are indicator variables equal to one if an environmental, social, or governance issue is covered, respectively, and zero otherwise. Control variables are defined in Appendix E. Regressions include year and two-digit SIC code industry fixed effects and standard errors clustered by firm. Numbers in parentheses are *t*-statistics. Statistical significance is indicated by ***, **, and * for 1%, 5%, and 10%, respectively. For coefficients that are consistent with predictions, significance is one-tailed.

Table 2.5 Client negative media coverage and auditor resignations

	Predicted sign	(1) *RESIGNED*	(2) *RESIGNED*	(3) *RESIGNED*	(4) *RESIGNED*
NEG_MEDIA	+	0.166**			
		(1.75)			
E_ISSUE	+		-0.450		
			(-0.41)		
S_ISSUE	+			-0.737	
				(-0.66)	
G_ISSUE	+				2.006***
					(3.33)
LNASSETS	+	-0.075	-0.029	-0.019	-0.111
		(-0.24)	(-0.09)	(-0.06)	(-0.34)
ROA	-	1.818	1.721	1.735	2.066
		(1.04)	(0.99)	(0.99)	(1.20)
LEVERAGE	+	-1.489	-1.475	-1.480	-1.414
		(-1.00)	(-1.01)	(-1.00)	(-1.01)
SALESGROWTH	+	-0.073	-0.093	-0.091	-0.072
		(-0.18)	(-0.21)	(-0.21)	(-0.18)
ZSCORE	+	-0.015	-0.014	-0.014	0.002
		(-0.16)	(-0.16)	(-0.16)	(0.03)
MA	+	0.069	0.045	0.035	0.014
		(0.15)	(0.10)	(0.08)	(0.03)
FOREIGN	+	0.082	0.069	0.066	0.123
		(0.13)	(0.11)	(0.10)	(0.19)
P_SCORE	+	-2.650*	-2.647*	-2.651*	-2.646*
		(-2.18)	(-2.17)	(-2.17)	(-2.21)
RESTATEMENT	+	0.973**	0.957**	0.955**	0.938**
		(1.74)	(1.73)	(1.72)	(1.68)
GC	+	1.608***	1.651***	1.676***	1.641***
		(2.53)	(2.63)	(2.69)	(2.57)
LOGAUDITFEES	-	-0.653	-0.625	-0.625	-0.686*
		(-1.23)	(-1.20)	(-1.19)	(-1.37)
INDUSTRYEXP	-	1.257	1.243	1.258	1.501
		(1.66)	(1.62)	(1.62)	(1.84)
Industry and year fixed effects		Included	Included	Included	Included
Constant		1.259	0.822	0.737	2.192
		(0.19)	(0.13)	(0.11)	(0.38)
Observations		4,376	4,376	4,376	4,376
Pseudo R^2		0.178	0.176	0.177	0.199

This table reports results of logit regressions estimating the impact of client negative media coverage on the likelihood of auditor resignation. The test variables in Columns (1)-(4) are *NEG_MEDIA*, *E_ISSUE, S_ISSUE,* and *G_ISSUE*, respectively. *NEG_MEDIA* is the maximum client negative media coverage of ESG practices during the audit negotiation period (fourth quarter of *t*-1 and first quarter of *t*), adjusted by the negotiation period mean. *E_ISSUE, S_ISSUE,* and *G_ISSUE* are indicator variables equal to one if an environmental, social, or governance issue is covered, respectively, and zero otherwise. Control variables are defined in Appendix E. Regressions include year and two-digit SIC code industry fixed effects and standard errors clustered by firm. Numbers in parentheses are *t*-statistics. Statistical significance is indicated by ***, **, and * for 1%, 5%, and 10%, respectively. For coefficients that are consistent with predictions, significance is one-tailed.

Table 2.6 Client negative media coverage and audit fees

Panel A: Main results

	Predicted sign	(1) *LOGAUDIT FEES*	(2) *LOGAUDIT FEES*	(3) *LOGAUDIT FEES*	(4) *LOGAUDIT FEES*
NEG_MEDIA	+	0.026***			
		(4.79)			
E_ISSUE	+		0.122***		
			(4.64)		
S_ISSUE	+			0.099***	
				(4.15)	
G_ISSUE	+				0.145***
					(5.68)
LNASSETS	+	0.528***	0.531***	0.531***	0.530***
		(55.30)	(56.17)	(55.37)	(57.28)
ROA	-	-0.330***	-0.330***	-0.333***	-0.322***
		(-3.32)	(-3.31)	(-3.34)	(-3.24)
LEVERAGE	+	-0.100	-0.106	-0.105	-0.103
		(-1.13)	(-1.20)	(-1.19)	(-1.16)
SALESGROWTH	+	-0.004	-0.004	-0.004	-0.004
		(-0.83)	(-0.84)	(-0.86)	(-0.91)
ZSCORE	+	0.025***	0.025***	0.025***	0.026***
		(2.68)	(2.68)	(2.67)	(2.76)
MA	+	0.072***	0.071***	0.073***	0.068***
		(3.61)	(3.55)	(3.63)	(3.38)
FOREIGN	+	0.119***	0.118***	0.120***	0.121***
		(5.14)	(5.11)	(5.19)	(5.25)
FYE_DEC	+	0.039	0.039	0.040	0.040
		(1.17)	(1.17)	(1.21)	(1.23)
SEGMENTS	+	0.081***	0.080***	0.080***	0.081***
		(6.45)	(6.40)	(6.39)	(6.47)
P_SCORE	+	0.437***	0.427***	0.427***	0.428***
		(3.85)	(3.77)	(3.76)	(3.78)
RESTATEMENT	+	0.031*	0.030	0.030	0.031
		(1.28)	(1.26)	(1.25)	(1.26)
GC	-	-0.046	-0.041	-0.044	-0.041
		(-0.52)	(-0.46)	(-0.50)	(-0.46)
MW	+	0.295***	0.293***	0.294***	0.290***
		(6.94)	(6.91)	(6.96)	(6.87)
INDUSTRYEXP	+	-0.012	-0.015	-0.012	-0.010
		(-0.26)	(-0.32)	(-0.27)	(-0.22)
Industry and year fixed effects		Included	Included	Included	Included
Constant		11.124***	11.120***	11.123***	11.111***
		(35.10)	(34.14)	(35.21)	(35.50)
Observations		7,528	7,528	7,528	7,528
Adjusted R^2		0.818	0.818	0.818	0.819

Coefficient comparisons	Chi2	*p*-value
E_ISSUE vs. *S_ISSUE*	1.42	0.2340
E_ISSUE vs. *G_ISSUE*	0.69	0.4069
S_ISSUE vs. *G_ISSUE*	3.05	0.0808

Table 2.6 (continued)

Panel B: Change model of main pricing result

	Predicted sign	(1) *ΔLOGAUDITFEES*	
ΔNEG_MEDIA	+	0.003**	(1.88)
ΔLNASSETS	+	0.000	(0.03)
ΔROA	+	-0.029	(-0.99)
ΔLEVERAGE	+	0.144***	(3.27)
ΔSALESGROWTH	+	0.053***	(4.08)
ΔZSCORE	-	0.016**	(4.10)
ΔMA	+	-0.020**	(-3.24)
ΔFOREIGN	+	-0.005	(-0.93)
ΔFYE_DEC	+	-0.288***	(-2.54)
ΔSEGMENTS	+	0.019***	(2.04)
ΔP_SCORE	+	0.098***	(2.62)
ΔRESTATEMENT	+	0.015**	(1.67)
ΔGC	+	-0.063*	(-2.19)
ΔMW	+	0.100***	(5.91)
ΔINDUSTRYEXP	+	0.008	(0.47)
Industry and year fixed effects		Included	
Constant		0.063***	(4.01)
Observations		6,393	
Adjusted R^2		0.099	

Panel C: Reputation risk peaks and audit pricing

	Predicted sign	(1) *LOGAUDIT FEES*	(2) *LOGAUDIT FEES*	(3) *LOGAUDIT FEES*
NEGMEDIA_PEAK_PRIOR	?	0.015		
		(0.15)		
NEGMEDIA_PEAK_NEGOT	+		0.106**	
			(1.83)	
NEGMEDIA_PEAK_SUBSEQ	+			0.046**
				(1.90)
All controls from Panel A		Included	Included	Included
Constant		10.632***	10.239***	10.341***
		(26.70)	(26.56)	(28.91)
Observations		1,090	1,275	1,625
Adjusted R^2		0.791	0.789	0.780

This table reports results of multivariate regressions estimating the impact of client negative media coverage on audit fees. The dependent variable in Panel A is the natural logarithm of audit fees. The test variables in Columns (1)-(4) are *NEG_MEDIA*, *E_ISSUE, S_ISSUE,* and *G_ISSUE*, respectively. *NEG_MEDIA* is the maximum client negative media coverage of ESG practices during the audit negotiation period (fourth quarter of *t*-1 and first quarter of *t*), adjusted by the negotiation period mean. *E_ISSUE, S_ISSUE,* and *G_ISSUE* are indicator variables equal to one if an environmental, social, or governance issue is covered, respectively, and zero otherwise. Panel B reports results of a one-year change model, where all variables are calculated by subtracting the value in *t*-1 from the value in *t*. Panel C reports results from testing the association between various coverage peaks and *LOGAUDITFEES.* For the sake of presentation, all controls from Panel A are included in the estimation of Panel C but are not tabled. *NEGMEDIA_PEAK_PRIOR* is an indicator variable equal to one if the index within the first through third quarters of *t*-1 is above the 60th percentile and if the index within the fourth quarter of *t*-1 and throughout year t is below the 40th percentile, and zero otherwise. *NEGMEDIA_PEAK_NEGOT* is an indicator variable equal to one if the index within the fourth quarter of *t*-1 and the first quarter of *t* is above the 60th percentile and if the index within the second through fourth quarters of year *t* is below the 40th percentile, and zero otherwise. *NEGMEDIA_PEAK_SUBSEQ* is an indicator variable equal to one if the index within the second through fourth quarters of year *t* is above the 60th percentile and if the index within the fourth quarter of *t*-1 and the first quarter of *t* is below the 40th percentile. For all panels, control variables are defined in Appendix E. Regressions include year and two-digit SIC code industry fixed effects and standard errors clustered by firm. Numbers in parentheses are *t*-statistics. Statistical significance is indicated by ***, **, and * for 1%, 5%, and 10%, respectively. For coefficients that are consistent with predictions, significance is one-tailed.

Table 2.7 Supplemental: Reaction to reach of media sources

	Predicted sign	(1) *LOGAUDITFEES*	(2) *LOGAUDITFEES*
LOWHIGH_SUM_LEAD	?	0.038	
		(1.35)	
LOWHIGH_SUM	+		0.045**
			(1.88)
LNASSETS	+	0.535***	0.537***
		(55.73)	(58.50)
ROA	-	-0.297***	-0.341***
		(-2.85)	(-3.41)
LEVERAGE	+	-0.106	-0.112
		(-1.14)	(-1.26)
SALESGROWTH	+	-0.006	-0.004
		(-1.07)	(-0.86)
ZSCORE	+	0.026***	0.025***
		(2.69)	(2.69)
MA	+	0.075***	0.068***
		(3.42)	(3.36)
FOREIGN	+	0.127***	0.122***
		(5.11)	(5.25)
FYE_DEC	+	0.038	0.040
		(1.11)	(1.21)
SEGMENTS	+	0.082***	0.081***
		(6.25)	(6.43)
P_SCORE	+	0.440***	0.433***
		(3.69)	(3.77)
RESTATEMENT	+	0.008	0.031
		(0.30)	(1.27)
GC	-	-0.042	-0.038
		(-0.43)	(-0.42)
MW	+	0.329***	0.295***
		(7.02)	(7.00)
INDUSTRYEXP	+	-0.012	-0.013
		(-0.25)	(-0.28)
Industry and year fixed effects		Included	Included
Constant		11.093***	11.120***
		(32.61)	(33.84)
Observations		6,326	7,528
Adjusted R^2		0.811	0.817

This table reports results of regressions estimating the association between issue elevation from low to high reach media sources and *LOGAUDITFEES*. *LOWHIGH_SUM_LEAD* is a count variable of ESG issues that move from a low reach media source in *t* to a high reach media source in *t*+1. *LOWHIGH_*SUM is a count variable of ESG issues that move from a low reach media source in *t*-1 to a high reach media source in *t*. Control variables are defined in Appendix E and consistent with those used in Table 2.6. Regressions include year and two-digit SIC code industry fixed effects and standard errors clustered by firm. Numbers in parentheses are *t*-statistics. Statistical significance is indicated by ***, **, and * for 1%, 5%, and 10%, respectively. For coefficients that are consistent with predictions, significance is one-tailed.

Table 2.8 Supplemental: Sample isolations

Panel A: Auditor resignations

	Predicted sign	(1) *Failed Benford removed* *RESIGNED*	(2) *Top quartile of p-score removed* *RESIGNED*	(3) *Negative change in sales removed* *RESIGNED*	(4) *Negative stock returns removed* *RESIGNED*
NEG_MEDIA	+	0.232***	0.195**	0.271***	0.229**
		(2.18)	(1.67)	(2.68)	(1.77)
All controls from Table 2.5		Included	Included	Included	Included
Constant		-0.231	0.931	5.128	-0.467
		(-0.03)	(0.12)	(0.60)	(-0.04)
Observations		2,461	3,281	2,118	1,100
Pseudo R^2		0.208	0.190	0.203	0.236

Panel B: Audit fees

	Predicted sign	(1) *Failed Benford removed* *LOGAUDIT FEES*	(2) *Top quartile of p-score removed* *LOGAUDIT FEES*	(3) *Negative change in sales removed* *LOGAUDIT FEES*	(4) *Negative stock returns removed* *LOGAUDIT FEES*
NEG_MEDIA	+	0.027***	0.028***	0.024***	0.020***
		(4.80)	(4.69)	(4.30)	(3.16)
All controls from Table 2.6, Panel A		Included	Included	Included	Included
Constant		11.163***	11.026***	11.123***	10.899***
		(38.25)	(32.13)	(32.57)	(33.72)
Observations		6,347	5,643	5,250	3,774
Adjusted R^2		0.818	0.826	0.811	0.830

This table reports results re-estimating our main results within isolated samples. Panel A reports results of logit regressions estimating the association of *NEG_MEDIA* with the likelihood of auditor change. Panel B reports results of multivariate regressions estimating the association of *NEG_MEDIA* with the natural logarithm of audit fees. The sample used in Column (1) excludes firms where *BENFORD_FAIL* is equal to one. The sample used in Column (2) excludes firms with P_SCORE in the top quartile. The sample used in Column (3) excludes firms where sales decrease from *t*-1 to *t*. The sample used in Column (4) excludes firms where *STOCKRETURN* is negative. In all columns, *NEG_MEDIA* is the maximum client negative media coverage of ESG practices during the audit negotiation period (fourth quarter of *t*-1 and first quarter of *t*), adjusted by the negotiation period mean. For the sake of presentation, all controls from Tables 2.5 and 2.6 are included in the estimations but not tabled. Regressions include year and two-digit SIC code industry fixed effects and standard errors clustered by firm. Numbers in parentheses are *t*-statistics. Statistical significance is indicated by ***, **, and * for 1%, 5%, and 10%, respectively. For coefficients that are consistent with predictions, significance is one-tailed.

Table 2.9 Supplemental: Abnormal audit fees

	Predicted sign	(1) *ABFEE*	(2) *ABFEE*	(3) *ABFEE*	(4) *ABFEE*
NEG_MEDIA	+	0.023***			
		(4.57)			
E_ISSUE	+		0.107***		
			(4.45)		
S_ISSUE	+			0.093***	
				(4.18)	
G_ISSUE	+				0.131***
					(5.69)
LNASSETS	+	-0.016	-0.013	-0.014	-0.014
		(-1.93)	(-1.61)	(-1.61)	(-1.75)
ROA	-	0.251**	0.250**	0.248**	0.258**
		(2.83)	(2.81)	(2.79)	(2.92)
LEVERAGE	+	-0.107	-0.113	-0.112	-0.110
		(-1.33)	(-1.40)	(-1.38)	(-1.36)
SALESGROWTH	+	0.001	0.001	0.001	0.001
		(0.26)	(0.22)	(0.19)	(0.15)
ZSCORE	+	0.029***	0.030***	0.029***	0.030***
		(3.47)	(3.48)	(3.47)	(3.56)
MA	+	0.077***	0.076***	0.078***	0.074***
		(4.26)	(4.21)	(4.30)	(4.04)
FOREIGN	+	0.091***	0.090***	0.092***	0.093***
		(4.20)	(4.18)	(4.26)	(4.31)
FYE_DEC	+	-0.003	-0.003	-0.002	-0.002
		(-0.10)	(-0.10)	(-0.07)	(-0.05)
SEGMENTS	+	0.002	0.001	0.001	0.002
		(0.14)	(0.11)	(0.10)	(0.16)
P_SCORE	+	0.018	0.010	0.010	0.011
		(0.17)	(0.09)	(0.09)	(0.10)
RESTATEMENT	+	-0.024	-0.025	-0.025	-0.024
		(-1.10)	(-1.13)	(-1.12)	(-1.10)
GC	-	-0.038	-0.033	-0.037	-0.034
		(-0.47)	(-0.42)	(-0.46)	(-0.41)
MW	+	0.237***	0.236***	0.236***	0.233***
		(5.98)	(5.95)	(5.98)	(5.89)
INDUSTRYEXP	+	-0.029	-0.031	-0.029	-0.027
		(-0.67)	(-0.72)	(-0.67)	(-0.62)
Industry and year fixed effects		Included	Included	Included	Included
Constant		-0.027	-0.031	-0.028	-0.038
		(-0.10)	(-0.11)	(-0.11)	(-0.15)
Observations		7,513	7,513	7,513	7,513
Adjusted R^2		0.028	0.027	0.026	0.029

Coefficient comparisons	Chi2	*p*-value
E_ISSUE vs. *S_ISSUE*	0.63	0.4259
E_ISSUE vs. *G_ISSUE*	0.94	0.3320
S_ISSUE vs. *G_ISSUE*	2.75	0.0975

This table reports results of multivariate regressions estimating the impact of client negative media coverage on abnormal audit fees, which is defined as the difference between the actual and fitted values of audit fees estimated as a function of misstatement risk and other control variables (following the model in Lobo and Zhao (2013)). The test variables in Columns (1)-(4) are *NEG_MEDIA*, *E_ISSUE, S_ISSUE,* and *G_ISSUE*, respectively. Control variables are defined in Appendix E. Regressions include year and two-digit SIC code industry fixed effects and standard errors clustered by firm. Numbers in parentheses are *t*-statistics. Statistical significance is indicated by ***, **, and * for 1%, 5%, and 10%, respectively. For coefficients that are consistent with predictions, significance is one-tailed.

Table 2.10 Supplemental: Negative media coverage, business risk, and financial reporting failures

Panel A: Within full sample

	Predicted sign	(1) *NEW_GC*	(2) *MISSTATEMENT*	(3) *MW*	(4) *DACC*
NEG_MEDIA	?/?/?/?	-0.010	0.001	0.055	0.000
		(-0.07)	(0.05)	(1.32)	(0.49)
LNASSETS	-/-/-/-	0.574**	-0.043	-0.276***	-0.002***
		(3.33)	(-0.83)	(-4.07)	(-2.15)
LEVERAGE	-/+/+/+	-3.412***	0.555***	0.154	-0.007
		(-2.07)	(2.01)	(0.40)	(-1.22)
OANCF	-/-/-/+	-0.000	-0.000***	-0.000***	0.000***
		(-0.09)	(-2.64)	(-3.38)	(3.46)
ROA	-/-/-/-	-3.293***	-0.476	-1.227***	-0.051***
		(-2.74)	(-1.26)	(-3.18)	(-3.94)
BIG4	-/+/-/-	-1.467***	0.391**	-0.505***	0.001
		(-2.31)	(1.92)	(-2.52)	(0.37)
AUDITORCHANGE	+/+/+/+	0.000	0.270*	1.023***	0.009*
		(N/A)	(1.39)	(5.43)	(1.49)
STD_CASH_5YR	+/+/+/+	-8.080	0.082	-1.246	0.304***
		(-1.40)	(0.07)	(-1.39)	(6.90)
STD_SALES_5YR	+/+/+/+	1.402*	0.816***	1.063***	0.009*
		(1.32)	(3.07)	(2.98)	(1.51)
FIRM_AGE	-/-/-/-	-0.043***	0.001	-0.002	-0.000***
		(-2.06)	(0.13)	(-0.31)	(-4.42)
LIT_RISK	+/+/+/+	12.877***	-0.592	2.200**	-0.006
		(11.60)	(-0.75)	(1.84)	(-0.42)
GC	+/+/+		0.067	0.639**	0.032**
			(0.20)	(1.92)	(1.72)
ZSCORE	+	0.747***			
		(3.05)			
TACC	+				0.000***
					(2.49)
Industry and year fixed effects		Included	Included	Included	Included
Constant		-6.727***	-1.918**	0.951	0.061***
		(-3.40)	(-2.49)	(0.68)	(5.58)
Observations		672	7,217	6,652	6,570
Pseudo/Adjusted R^2		0.331	0.051	0.148	0.211

Table 2.10 (continued)

Panel B: Within firm-year observations where fees decline or do not change

	Predicted sign	(1) *NEW_GC*	(2) *MISSTATEMENT*	(3) *MW*	(4) *DACC*
NEG_MEDIA	?/?/?/?	-0.297	0.016	0.011	0.000
		(-0.73)	(0.36)	(0.15)	(0.30)
Controls from Panel A		Included	Included	Included	Included
Constant		-12.381***	-2.485**	1.910	0.049***
		(-2.61)	(-2.10)	(1.14)	(4.07)
Observations		290	3,183	2,757	2,779
Pseudo/Adjusted R^2		0.411	0.059	0.157	0.268

This table reports results from regressions of *NEG_MEDIA* on four measures of client negative media coverage and financial reporting quality. The dependent variables in columns (1)-(4) are *NEW_GC, MISSTATEMENT, MW,* and *DACC*, respectively. *NEG_MEDIA* is the maximum client negative media coverage of ESG practices during the audit negotiation period (fourth quarter of *t*-1 and first quarter of *t*), adjusted by the negotiation period mean. *NEW_GC* is an indicator variable equal to one for companies with a going concern opinion that did not receive this opinion in the prior year, and zero otherwise. For this analysis, the sample is limited to distressed firms (i.e., those with negative net operating cash flows or negative net income in *t*) and firms in financial industries are removed. *MISSTATEMENT* is an indicator variable equal to one for companies with a misstatement in the current period that subsequently led to a restatement, and zero otherwise. *MW* is an indicator variable equal to one if the firm discloses a material weakness and zero otherwise. *DACC* is discretionary accruals calculated from the modified Jones model with control for firm performance. Control variables are defined in Appendix E. For presentation sake, we use select control variables that are consistent predictors of all four dependent variables. Untabulated results with common sets of control variables remain consistent. Panel A estimates these regressions within the full sample, while Panel B removes firm-year observations where audit fees increase in that year. For the sake of presentation, all controls from Panel A are included in the estimation of Panel B but are not tabled Regressions include year and two-digit SIC code industry fixed effects and standard errors clustered by firm. Numbers in parentheses are *t*-statistics. Statistical significance is indicated by ***, **, and * for 1%, 5%, and 10%, respectively. For coefficients that are consistent with predictions, significance is one-tailed.

Table 3.1 Sample distribution

Year	Observations	CEO dismissal	Internal appointments	External appointments
2007	1,032	38	23	15
2008	1,080	39	26	13
2009	1,091	45	29	15
2010	1,072	43	28	15
2011	1,052	59	43	14
2012	991	39	24	15
2013	965	24	14	9
2014	942	29	15	12
2015	802	18	9	4
Firm-year observations	**9,027**	**334**	**211**	**112**

Table 3.2 Descriptive statistics

Panel A: Summary statistics

	Number of observations	Mean	Median	Standard deviation	25th percentile	75th percentile
Media measures						
NEG_MEDIA	9,027	14.401	11.000	15.537	0.000	26.000
E_ISSUE	9,027	0.189	0.000	0.391	0.000	0.000
S_ISSUE	9,027	0.255	0.000	0.436	0.000	1.000
G_ISSUE	9,027	0.194	0.000	0.395	0.000	0.000
Dependent variables						
CEO_DISMISSAL	9,027	0.037	0.000	0.189	0.000	0.000
INTERNAL_CEO	323	0.653	1.000	0.477	0.000	1.000
EXTERNAL_CEO	323	0.347	0.000	0.477	0.000	1.000
Control variables						
ROA	9,027	0.028	0.043	0.123	0.013	0.081
STOCKRETURN	9,027	0.057	-0.004	0.483	-0.194	0.207
CEO_AGE	9,027	56.475	56.000	7.186	52.000	61.000
LNASSETS	9,027	7.988	7.987	1.793	6.858	9.139
SEGMENTS	9,027	1.794	1.000	1.071	1.000	2.000
BOARD_INDEP	9,027	0.789	0.833	0.130	0.714	0.889
BOARD_SIZE	9,027	9.322	9.000	2.252	8.000	11.000
RESTATEMENT	9,027	0.076	0.000	0.265	0.000	0.000
MW	9,027	0.031	0.000	0.174	0.000	0.000
TALENT	334	0.548	1.000	0.498	0.000	1.000
HEIR_APPARENT	334	0.302	0.000	0.460	0.000	1.000

Panel B: Correlation matrix

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
(1) *NEG_MEDIA*	1						
(2) *E_ISSUE*	0.584***	1					
(3) *S_ISSUE*	0.689***	0.589***	1				
(4) *G_ISSUE*	0.608***	0.314***	0.377***	1			
(5) *CEO_DISMISSAL*	0.027**	0.003	0.004	0.049***	1		
(6) *ROA*	0.083***	0.037***	0.073***	0.055***	-0.055***	1	
(7) *STOCKRETURN*	-0.065***	-0.046***	-0.045***	-0.043***	-0.057***	0.174***	1
(8) *LNASSETS*	0.474***	0.382***	0.409***	0.373***	-0.023*	0.240***	-0.012

* $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Table 3.2 (continued)

Panel C: Further detail on frequency of ESG issues

Sample for CEO dismissal analyses

	***CEO_DISMISSAL* = 0 (N = 8,693)**		***CEO_DISMISSAL* = 1 (N = 334)**	
E_ISSUE	1,638	(18.84%)	65	(19.46%)
Low severity and low reach	261	(3.00%)	13	(3.89%)
High severity and low reach	182	(2.09%)	7	(2.10%)
Low severity and high reach	499	(5.74%)	11	(3.29%)
High severity and high reach	695	(7.99%)	34	(10.18%)
S_ISSUE	2,215	(25.48%)	88	(26.35%)
Low severity and low reach	318	(3.66%)	14	(4.19%)
High severity and low reach	242	(2.78%)	5	(1.50%)
Low severity and high reach	659	(7.58%)	24	(7.19%)
High severity and high reach	994	(11.43%)	45	(13.47%)
G_ISSUE	1,651	(18.99%)	98	(29.34%)
Low severity and low reach	197	(2.27%)	6	(1.80%)
High severity and low reach	120	(1.38%)	3	(0.90%)
Low severity and high reach	741	(8.52%)	55	(16.47%)
High severity and high reach	591	(6.80%)	34	(10.18%)

Sample for CEO succession analyses

	***INTERNAL_CEO* = 1 (N = 211)**		***EXTERNAL_CEO* = 1 (N = 112)**	
E_ISSUE	47	(22.27%)	16	(14.29%)
Low severity and low reach	8	(3.79%)	4	(3.57%)
High severity and low reach	5	(2.37%)	2	(1.79%)
Low severity and high reach	7	(3.32%)	4	(3.57%)
High severity and high reach	27	(12.80%)	6	(5.36%)
S_ISSUE	58	(27.49%)	27	(24.11%)
Low severity and low reach	8	(3.79%)	4	(3.57%)
High severity and low reach	1	(0.47%)	4	(3.57%)
Low severity and high reach	16	(7.58%)	7	(6.25%)
High severity and high reach	33	(15.64%)	12	(10.71%)
G_ISSUE	58	(27.49%)	38	(33.93%)
Low severity and low reach	3	(1.42%)	3	(2.68%)
High severity and low reach	2	(0.95%)	1	(0.89%)
Low severity and high reach	33	(15.64%)	21	(18.75%)
High severity and high reach	20	(9.48%)	13	(11.61%)

Table 3.3 Negative media coverage and CEO dismissal

	(1) *CEO_ DISMISSAL*	(2) *CEO_ DISMISSAL*	(3) *CEO_ DISMISSAL*	(4) *CEO_ DISMISSAL*
NEG_MEDIA	0.017***			
	(4.05)			
E_ISSUE		0.277*		
		(1.70)		
S_ISSUE			0.220	
			(1.57)	
G_ISSUE				0.864***
				(5.75)
ROA	-1.420***	-1.488***	-1.500***	-1.349***
	(-3.32)	(-3.46)	(-3.51)	(-3.16)
STOCKRETURN	-0.770***	-0.806***	-0.806***	-0.777***
	(-3.13)	(-3.23)	(-3.22)	(-3.16)
CEO_AGE	0.028***	0.028***	0.028***	0.029***
	(3.41)	(3.38)	(3.39)	(3.50)
LNASSETS	-0.108**	-0.063	-0.063	-0.121**
	(-2.03)	(-1.20)	(-1.19)	(-2.31)
SEGMENTS	-0.013	-0.010	-0.010	-0.002
	(-0.19)	(-0.15)	(-0.14)	(-0.03)
BOARD_INDEP	0.103	0.176	0.178	0.155
	(0.23)	(0.39)	(0.40)	(0.34)
BOARD_SIZE	0.086**	0.093***	0.094***	0.089**
	(2.45)	(2.69)	(2.71)	(2.51)
RESTATEMENT	-0.107	-0.110	-0.114	-0.132
	(-0.46)	(-0.47)	(-0.49)	(-0.57)
MW	0.531*	0.565**	0.561**	0.514*
	(1.94)	(2.06)	(2.05)	(1.87)
Industry and year fixed effects	Included	Included	Included	Included
Constant	-4.760***	-4.936***	-4.913***	-4.648***
	(-4.97)	(-5.19)	(-5.22)	(-4.87)
Observations	8,838	8,838	8,838	8,838
Pseudo R^2	0.061	0.057	0.057	0.067

Coefficient comparisons	Chi2	*p*-value
E_ISSUE vs. *S_ISSUE*	0.12	0.7319
E_ISSUE vs. *G_ISSUE*	7.93	0.0049
S_ISSUE vs. *G_ISSUE*	12.16	0.0005

This table reports results of logit regressions estimating the impact of negative media coverage on the likelihood of CEO dismissal (*CEO_DISMISSAL*). The test variables in Columns (1)-(4) are *NEG_MEDIA*, *E_ISSUE*, *S_ISSUE*, and *G_ISSUE*, respectively. *NEG_MEDIA* is the maximum negative media coverage of ESG practices within the twelve months prior to the CEO turnover date for firm-year observations with a CEO dismissal, and within the fiscal year for firm-year observations without a CEO dismissal. *E_ISSUE*, *S_ISSUE*, and *G_ISSUE* are indicator variables equal to one if an environmental, social, or governance issue is covered within the specified periods, respectively, and zero otherwise. Control variables are defined in Appendix F. Regressions include year and industry (Fama-French 48 classification) fixed effects and standard errors are clustered by firm. Numbers in parentheses are t-statistics. Two-tailed statistical significance is indicated by ***, **, and * for 1%, 5%, and 10%, respectively.

Table 3.4 Severity and reach of ESG issues covered in the media and CEO dismissal

	Environment			Social			Governance		
	(1) *CEO_DISMISSAL*	(2) *CEO_DISMISSAL*	(3) *CEO_DISMISSAL*	(4) *CEO_DISMISSAL*	(5) *CEO_DISMISSAL*	(6) *CEO_DISMISSAL*	(7) *CEO_DISMISSAL*	(8) *CEO_DISMISSAL*	(9) *CEO_DISMISSAL*
	Indicators represent environmental issues			**Indicators represent social issues**			**Indicators represent governance issues**		
LOW_REACH	0.308			0.007			0.098		
	(1.22)			(0.03)			(0.27)		
HIGH_REACH	0.264			0.305*			0.999***		
	(1.35)			(1.84)			(6.46)		
LOW_SEV		0.020			0.245			0.917***	
		(0.08)			(1.28)			(5.53)	
HIGH_SEV		0.495**			0.200			0.769***	
		(2.44)			(1.08)			(3.64)	
LOWSEV_LOWREACH			0.364			0.300			0.113
			(1.20)			(1.03)			(0.26)
HIGHSEV_LOWREACH			0.250			-0.520			0.062
			(0.61)			(-1.12)			(0.10)
LOWSEV_HIGHREACH			-0.256			0.189			1.045***
			(-0.79)			(0.82)			(6.04)
HIGHSEV_HIGHREACH			0.554**			0.392**			0.917***
			(2.49)			(1.99)			(4.15)
ROA	-1.489***	-1.474***	-1.473***	-1.491***	-1.501***	-1.472***	-1.382***	-1.351***	-1.385***
	(-3.61)	(-3.58)	(-3.57)	(-3.62)	(-3.65)	(-3.57)	(-3.35)	(-3.28)	(-3.35)
STOCKRETURN	-0.805***	-0.802***	-0.800***	-0.805***	-0.806***	-0.806***	-0.770***	-0.780***	-0.772***
	(-4.68)	(-4.67)	(-4.66)	(-4.68)	(-4.68)	(-4.68)	(-4.51)	(-4.55)	(-4.52)
CEO_AGE	0.028***	0.028***	0.028***	0.028***	0.028***	0.028***	0.029***	0.029***	0.029***
	(3.55)	(3.53)	(3.56)	(3.56)	(3.57)	(3.56)	(3.70)	(3.70)	(3.71)
LNASSETS	-0.062	-0.072	-0.071	-0.068	-0.062	-0.072	-0.126***	-0.118**	-0.123***
	(-1.32)	(-1.51)	(-1.50)	(-1.42)	(-1.30)	(-1.50)	(-2.67)	(-2.48)	(-2.59)
SEGMENTS	-0.010	-0.009	-0.009	-0.010	-0.010	-0.013	-0.003	-0.001	-0.002
	(-0.17)	(-0.14)	(-0.15)	(-0.17)	(-0.16)	(-0.22)	(-0.04)	(-0.02)	(-0.03)
BOARD_INDEP	0.175	0.178	0.173	0.187	0.178	0.202	0.151	0.156	0.152
	(0.38)	(0.39)	(0.37)	(0.41)	(0.39)	(0.44)	(0.33)	(0.34)	(0.33)

Table 3.4 (continued)

	Environment			Social			Governance		
	(1) *CEO_DISMISSAL*	(2) *CEO_DISMISSAL*	(3) *CEO_DISMISSAL*	(4) *CEO_DISMISSAL*	(5) *CEO_DISMISSAL*	(6) *CEO_DISMISSAL*	(7) *CEO_DISMISSAL*	(8) *CEO_DISMISSAL*	(9) *CEO_DISMISSAL*
	Indicators represent environmental issues			**Indicators represent social issues**			**Indicators represent governance issues**		
BOARD_SIZE	0.093***	0.093***	0.093***	0.093***	0.094***	0.094***	0.089***	0.089***	0.089***
	(2.81)	(2.80)	(2.80)	(2.81)	(2.83)	(2.83)	(2.67)	(2.67)	(2.67)
RESTATEMENT	-0.110	-0.108	-0.100	-0.107	-0.114	-0.104	-0.124	-0.133	-0.125
	(-0.49)	(-0.48)	(-0.45)	(-0.48)	(-0.51)	(-0.47)	(-0.55)	(-0.59)	(-0.55)
MW	0.565**	0.566**	0.563**	0.566**	0.561**	0.564**	0.503*	0.515*	0.504*
	(2.12)	(2.12)	(2.11)	(2.12)	(2.10)	(2.11)	(1.86)	(1.91)	(1.87)
Industry and year fixed effects	Included	Included	Included	Included	Included	Included	Included	Included	Included
Constant	-4.935***	-4.964***	-4.963***	-4.931***	-4.908***	-4.972***	-4.628***	-4.641***	-4.626***
	(-5.00)	(-5.03)	(-5.02)	(-4.99)	(-4.97)	(-5.03)	(-4.65)	(-4.67)	(-4.65)
Observations	8,838	8,838	8,838	8,838	8,838	8,838	8,838	8,838	8,838
Pseudo R^2	0.057	0.058	0.059	0.057	0.057	0.058	0.070	0.067	0.070

This table reports results of logit regressions estimating the impact of various measures of negative media coverage of ESG issues on the likelihood of CEO dismissal (*CEO_DISMISSAL*). In Columns 1-3, environmental issues are disaggregated into the reach of media sources the issues were identified in (Column 1), the severity of the issues (Column 2), and a combination of reach and severity (Column 3). These variables are defined in Appendix F. In Columns 4-6, these indicator variables are disaggregated from social issues and in Columns 7-9 from governance issues. Control variables are defined in Appendix F. Regressions include year and industry (Fama-French 48 classification) fixed effects. Numbers in parentheses are t-statistics. Two-tailed statistical significance is indicated by ***, **, and * for 1%, 5%, and 10%, respectively.

Table 3.5 Negative media coverage and CEO successor origin

	(1) *EXTERNAL_CEO*	(2) *EXTERNAL_CEO*	(3) *EXTERNAL_CEO*	(4) *EXTERNAL_CEO*
NEG_MEDIA	0.012			
	(1.35)			
E_ISSUE		-0.247		
		(-0.60)		
S_ISSUE			0.220	
			(0.67)	
G_ISSUE				0.577*
				(1.73)
ROA	-2.138**	-2.221**	-2.196**	-2.091**
	(-2.40)	(-2.50)	(-2.46)	(-2.34)
STOCKRETURN	-0.628**	-0.642**	-0.637**	-0.638**
	(-2.03)	(-2.11)	(-2.06)	(-2.08)
CEO_AGE	-0.016	-0.015	-0.016	-0.016
	(-0.85)	(-0.81)	(-0.84)	(-0.86)
LNASSETS	0.123	0.172*	0.144	0.119
	(1.17)	(1.67)	(1.38)	(1.15)
SEGMENTS	0.058	0.063	0.054	0.046
	(0.44)	(0.47)	(0.41)	(0.36)
BOARD_INDEP	2.424*	2.368*	2.471**	2.347*
	(1.93)	(1.90)	(1.97)	(1.87)
BOARD_SIZE	-0.257***	-0.246***	-0.254***	-0.248***
	(-3.08)	(-2.95)	(-3.02)	(-2.97)
RESTATEMENT	0.116	0.069	0.069	0.111
	(0.20)	(0.12)	(0.12)	(0.19)
MW	0.915	0.953	0.971	0.895
	(1.29)	(1.33)	(1.33)	(1.27)
TALENT	0.387	0.317	0.371	0.395
	(1.24)	(1.01)	(1.19)	(1.30)
HEIR_APPARENT	0.408	0.389	0.387	0.409
	(1.33)	(1.25)	(1.24)	(1.31)
Industry and year fixed effects	Included	Included	Included	Included
Constant	-0.524	-0.827	-0.715	-0.476
	(-0.30)	(-0.47)	(-0.41)	(-0.28)
Observations	323	323	323	323
Pseudo R^2	0.113	0.110	0.110	0.116

This table reports results of logit regressions estimating the impact of negative media coverage on the likelihood of external CEO replacements (*EXTERNAL_CEO*). The sample is isolated to firm-year observations that have a CEO dismissal. The test variables in Columns (1)-(4) are *NEG_MEDIA*, *E_ISSUE*, *S_ISSUE*, and *G_ISSUE*, respectively. *NEG_MEDIA* is the maximum negative media coverage of ESG practices within the twelve months prior to the CEO turnover date for firm-year observations with a CEO dismissal, and within the fiscal year for firm-year observations without a CEO dismissal. *E_ISSUE*, *S_ISSUE*, and *G_ISSUE* are indicator variables equal to one if an environmental, social, or governance issue is covered within the specified periods, respectively, and zero otherwise. Control variables are defined in Appendix F. Regressions include year and industry (Fama-French 12 classification) fixed effects and standard errors clustered by firm. Numbers in parentheses are t-statistics. Two-tailed statistical significance is indicated by ***, **, and * for 1%, 5%, and 10%, respectively

Table 3.6 Severity and reach of ESG issues covered in the media and CEO successor origin

	Environment		Social		Governance	
	(1)	(2)	(3)	(4)	(5)	(6)
	EXTERNAL_CEO	*EXTERNAL_CEO*	*EXTERNAL_CEO*	*EXTERNAL_CEO*	*EXTERNAL_CEO*	*EXTERNAL_CEO*
	Indicators represent environmental issues		**Indicators represent social issues**		**Indicators represent governance issues**	
LOW_REACH	0.132		0.861		1.094	
	(0.22)		(1.47)		(1.32)	
HIGH_REACH	-0.456		-0.008		0.536	
	(-0.95)		(-0.02)		(1.59)	
LOW_SEV		0.014		0.098		0.442
		(0.03)		(0.22)		(1.20)
HIGH_SEV		-0.443		0.328		0.875*
		(-0.88)		(0.77)		(1.84)
ROA	-2.259**	-2.248**	-2.182**	-2.190**	-2.101**	-2.138**
	(-2.39)	(-2.37)	(-2.29)	(-2.31)	(-2.22)	(-2.25)
STOCKRETURN	-0.650*	-0.643*	-0.636*	-0.639*	-0.646*	-0.652*
	(-1.88)	(-1.86)	(-1.83)	(-1.84)	(-1.86)	(-1.88)
CEO_AGE	-0.014	-0.016	-0.015	-0.016	-0.016	-0.015
	(-0.74)	(-0.82)	(-0.78)	(-0.83)	(-0.85)	(-0.81)
LNASSETS	0.183*	0.179*	0.167	0.141	0.128	0.115
	(1.74)	(1.71)	(1.58)	(1.36)	(1.22)	(1.11)
SEGMENTS	0.056	0.063	0.051	0.054	0.039	0.037
	(0.44)	(0.50)	(0.40)	(0.43)	(0.31)	(0.29)
BOARD_INDEP	2.374*	2.358*	2.519**	2.473**	2.395*	2.304*
	(1.90)	(1.89)	(2.00)	(1.98)	(1.91)	(1.84)
BOARD_SIZE	-0.251***	-0.246***	-0.262***	-0.256***	-0.253***	-0.254***
	(-3.17)	(-3.12)	(-3.26)	(-3.21)	(-3.16)	(-3.19)
RESTATEMENT	0.093	0.068	-0.006	0.088	0.121	0.117
	(0.17)	(0.13)	(-0.01)	(0.17)	(0.23)	(0.22)
MW	0.955	0.955	1.025*	0.947	0.880	0.905
	(1.59)	(1.59)	(1.70)	(1.57)	(1.47)	(1.51)
TALENT	0.304	0.311	0.373	0.372	0.429	0.415
	(0.90)	(0.93)	(1.11)	(1.11)	(1.27)	(1.23)
HEIR_APPARENT	0.372	0.386	0.378	0.394	0.382	0.412
	(1.21)	(1.26)	(1.22)	(1.28)	(1.23)	(1.33)
Industry and year fixed effects	Included	Included	Included	Included	Included	Included
Constant	-0.895	-0.808	-0.902	-0.674	-0.510	-0.358
	(-0.51)	(-0.46)	(-0.51)	(-0.39)	(-0.29)	(-0.20)
Observations	323	323	323	323	323	323
Pseudo R^2	0.112	0.111	0.114	0.110	0.117	0.118

This table reports results of logit regressions estimating the impact of various measures of negative media coverage of ESG issues on the likelihood of external CEO replacements (*EXTERNAL_CEO*). The sample is isolated to firm-year observations that have a CEO dismissal. In Columns 1-2, environmental issues are disaggregated into the reach of media sources the issues were identified in (Column 1) and the severity of the issues (Column 2). These variables are defined in Appendix F. In Columns 3-4, these indicator variables are disaggregated from social issues and in Columns 5-6 from governance issues. Control variables are defined in Appendix F. Regressions include year and industry (Fama-French 12 classification) fixed effects. Numbers in parentheses are t-statistics. Two-tailed statistical significance is indicated by ***, **, and * for 1%, 5%, and 10%, respectively.

Table 3.7 CEO dismissal, CEO successor origin, and change in negative media coverage

	(1) ΔNEG_MEDIA	(2) ΔNEG_MEDIA	(3) ΔNEG_MEDIA	(4) ΔNEG_MEDIA
CEO_DISMISSAL	-5.710***		-7.276***	
	(-6.52)		(-7.13)	
EXTERNAL_CEO		-0.656		-1.198
		(-0.37)		(-0.51)
Δ*ROA*	-0.920	-6.337	0.891	0.711
	(-0.53)	(-0.86)	(0.49)	(0.06)
Δ*STOCKRETURN*	-0.607***	1.126	-0.462	3.706*
	(-2.69)	(0.90)	(-1.65)	(1.81)
CEO_AGE	-0.009	-0.065	0.019	0.222
	(-0.71)	(-0.49)	(0.65)	(1.17)
Δ*LNASSETS*	2.221***	2.991	1.259	4.661
	(2.99)	(0.71)	(1.35)	(1.17)
Δ*SEGMENTS*	-0.003	-2.602	-0.440	-3.012**
	(-0.01)	(-1.56)	(-0.93)	(-2.14)
Δ*BOARD_INDEP*	-1.218	-13.314	-3.528	1.619
	(-0.40)	(-1.15)	(-1.00)	(0.09)
Δ*BOARD_SIZE*	-0.175	0.224	-0.224	0.186
	(-1.00)	(0.29)	(-1.27)	(0.23)
Δ*RESTATEMENT*	0.326	-0.612	0.112	2.002
	(0.67)	(-0.25)	(0.23)	(0.60)
Δ*MW*	-0.205	2.535	0.398	-0.110
	(-0.26)	(0.61)	(0.50)	(-0.03)
TALENT		2.886		2.874
		(1.49)		(1.12)
HEIR_APPARENT		-0.704		-0.084
		(-0.33)		(-0.04)
Industry and year fixed effects	Included	Included	Included	Included
Constant	3.031*	2.088	2.029	-27.639**
	(1.89)	(0.22)	(0.61)	(-2.28)
Observations	7,319	260	3,408	136
Adjusted R^2	0.020	0.032	0.076	0.075

Coefficient comparisons	Chi2	*p*-value
CEO_DISMISSAL in Column (1) vs. Column (3)	3.65	0.0560
EXTERNAL_CEO in Column (2) vs. Column (4)	0.09	0.7641

This table reports results of a change model examining the impact of *CEO_DISMISSAL* and *EXTERNAL_CEO* on Δ*NEG_MEDIA*. For firm-year observations with CEO dismissal, this is measured as the index value twelve months after turnover less the maximum index value twelve months prior to turnover (i.e., the *NEG_MEDIA* value used in earlier analyses). For firm-year observations without a CEO dismissal, this is measured as the maximum index value in *t*+1 less the maximum index within *t* (i.e., the *NEG_MEDIA* value used in earlier analyses). All continuous control variables, with the exception of departing CEO age, are measured as the one-year change (year after turnover less year of turnover). Additionally, indicator variables for restatement and material weakness are measured as a one-year change. Control variables are defined in Appendix F. Regressions include year and industry (Fama-French 48 classification in Columns 1 and 3, Fama-French 12 classification in Columns 2 and 4) fixed effects and standard errors clustered by firm. Numbers in parentheses are t-statistics. Two-tailed statistical significance is indicated by ***, **, and * for 1%, 5%, and 10%, respectively.

Table 3.8 ESG-focused institutional ownership as an additional pressure

	(1) *CEO_ DISMISSAL*	(2) *CEO_ DISMISSAL*	(3) *CEO_ DISMISSAL*	(4) *CEO_ DISMISSAL*
NEG_MEDIA	0.022***			
	(3.24)			
E_ISSUE		0.569***		
		(2.78)		
S_ISSUE			0.463**	
			(2.55)	
G_ISSUE				0.681***
				(3.33)
ROA	-2.472***	-2.379***	-2.382***	-2.423***
	(-3.00)	(-2.81)	(-2.83)	(-2.92)
STOCKRETURN	-0.674	-0.706	-0.712	-0.699
	(-1.44)	(-1.50)	(-1.49)	(-1.48)
CEO_AGE	0.060***	0.058***	0.058***	0.060***
	(4.93)	(4.80)	(4.76)	(4.96)
LNASSETS	-0.214**	-0.163*	-0.166*	-0.192**
	(-2.38)	(-1.82)	(-1.82)	(-2.12)
SEGMENTS	0.063	0.060	0.075	0.076
	(0.72)	(0.68)	(0.84)	(0.85)
BOARD_INDEP	-0.282	-0.196	-0.210	-0.222
	(-0.39)	(-0.27)	(-0.28)	(-0.30)
BOARD_SIZE	0.117**	0.123**	0.125**	0.128***
	(2.35)	(2.47)	(2.52)	(2.58)
RESTATEMENT	-0.505	-0.502	-0.516	-0.461
	(-1.23)	(-1.23)	(-1.27)	(-1.14)
MW	0.618	0.642	0.656	0.654
	(1.06)	(1.11)	(1.14)	(1.13)
Industry and year fixed effects	Included	Included	Included	Included
Constant	-6.321***	-6.479***	-6.431***	-6.297***
	(-4.48)	(-4.69)	(-4.82)	(-4.53)
Observations	4,138	4,138	4,138	4,138
Pseudo R^2	0.085	0.082	0.081	0.085

Coefficient comparisons	Table 3.8 (isolated sample)	Table 3.3 (full sample)	Chi2	*p*-value
NEG_MEDIA	0.022*** (3.24)	0.017*** (4.05)	0.78	0.3767
E_ISSUE	0.569*** (2.78)	0.277* (1.70)	4.28	0.0386
S_ISSUE	0.463** (2.55)	0.220 (1.57)	3.32	0.0685
G_ISSUE	0.681*** (3.33)	0.864*** (5.75)	1.57	0.2106

This table reports results of logit regressions estimating the impact of negative media coverage on the likelihood of CEO dismissal (*CEO_DISMISSAL*), within a sample of firms held by two popular ESG-focused funds (Vanguard FTSE Social Index Fund and iShares MSCI KLD Social ETF). The test variables in Columns (1)-(4) are *NEG_MEDIA*, *E_ISSUE*, *S_ISSUE*, and *G_ISSUE*, respectively. *NEG_MEDIA* is the maximum negative media coverage of ESG practices within the twelve months prior to the CEO turnover date for firm-year observations with a CEO dismissal, and within the fiscal year for firm-year observations without a CEO dismissal. *E_ISSUE*, *S_ISSUE*, and *G_ISSUE* are indicator variables equal to one if an environmental, social, or governance issue is covered within the specified periods, respectively, and zero otherwise. Control variables are defined in Appendix F. Regressions include year and industry (Fama-French 48 classification) fixed effects and standard errors clustered by firm. Numbers in parentheses are t-statistics. Two-tailed statistical significance is indicated by ***, **, and * for 1%, 5%, and 10%, respectively

Table 3.9 Board characteristics as moderating variables

Panel A: Sustainability committee interactions

	(1) *CEO_ DISMISSAL*	(2) *CEO_ DISMISSAL*	(3) *CEO_ DISMISSAL*	(4) *CEO_ DISMISSAL*
NEG_MEDIA	0.020***			
	(4.15)			
E_ISSUE		0.336*		
		(1.89)		
S_ISSUE			0.138	
			(0.87)	
G_ISSUE				1.049***
				(6.45)
COMMITTEE	-0.101	-0.081	-0.153	0.160
	(-0.34)	(-0.27)	(-0.50)	(0.62)
*NEG_MEDIA * COMMITTEE*	0.019			
	(1.36)			
*E_ISSUE * COMMITTEE*		0.752*		
		(1.65)		
*S_ISSUE * COMMITTEE*			1.065**	
			(2.38)	
*G_ISSUE * COMMITTEE*				-0.069
				(-0.16)
Controls from Table 3.3	Included	Included	Included	Included
Constant	-4.740***	-4.757***	-4.784***	-4.310***
	(-4.23)	(-4.48)	(-4.46)	(-4.25)
Observations	6,937	6,937	6,937	6,937
Pseudo R^2	0.058	0.052	0.052	0.067

Panel B: Board size interactions

	(1) *CEO_ DISMISSAL*	(2) *CEO_ DISMISSAL*	(3) *CEO_ DISMISSAL*	(4) *CEO_ DISMISSAL*
NEG_MEDIA	0.018***			
	(4.20)			
E_ISSUE		0.270		
		(1.52)		
S_ISSUE			0.216	
			(1.44)	
G_ISSUE				0.941***
				(6.39)
BOARD_SIZE	0.090**	0.093***	0.094***	0.101***
	(2.55)	(2.66)	(2.69)	(2.87)
*NEG_MEDIA * BOARD_SIZE*	-0.001			
	(-0.94)			
*E_ISSUE * BOARD_SIZE*		0.007		
		(0.11)		
*S_ISSUE * BOARD_SIZE*			0.006	
			(0.10)	
*G_ISSUE * BOARD_SIZE*				-0.130**
				(-2.29)
Controls from Table 3.3	Included	Included	Included	Included
Constant	-4.817***	-4.929***	-4.907***	-4.818***
	(-5.09)	(-5.16)	(-5.21)	(-5.17)
Observations	8,838	8,838	8,838	8,838
Pseudo R^2	0.062	0.057	0.057	0.069

Table 3.9 (continued)

Panel C: Board busyness interactions

	(1) *CEO_ DISMISSAL*	(2) *CEO_ DISMISSAL*	(3) *CEO_ DISMISSAL*	(4) *CEO_ DISMISSAL*
NEG_MEDIA	0.017***			
	(4.02)			
E_ISSUE		0.248		
		(1.50)		
S_ISSUE			0.195	
			(1.39)	
G_ISSUE				0.875***
				(5.85)
BOARD_BUSY	0.121	0.023	0.091	0.171
	(0.65)	(0.12)	(0.50)	(0.94)
*NEG_MEDIA * BOARD_BUSY*	-0.008			
	(-0.78)			
*E_ISSUE * BOARD_BUSY*		0.489		
		(1.35)		
*S_ISSUE * BOARD_BUSY*			0.055	
			(0.15)	
*G_ISSUE * BOARD_BUSY*				-0.773*
				(-1.88)
Controls from Table 3.3	Included	Included	Included	Included
Constant	-4.703***	-4.781***	-4.824***	-4.602***
	(-4.85)	(-5.01)	(-5.09)	(-4.76)
Observations	8,793	8,793	8,793	8,793
Pseudo R^2	0.061	0.057	0.057	0.069

This table reports results replicating those in Table 3, with variables added for the interaction of negative media coverage measures (i.e., *NEG_MEDIA*, *E_ISSUE*, *S_ISSUE*, and *G_ISSUE*) and board characteristics. Panel A includes interactions with the presence of a sustainability committee. *COMMITTEE* is an indicator variable equal to one if a board-level committee focusing on sustainability-related issues exists, and zero otherwise. Panel B includes board size interactions; *BOARD_SIZE* is measured as the number of directors on the board during the fiscal-year. Panel C includes board busyness interactions; *BOARD_BUSY* is an indicator variable equal to one for firm-year observations where more than 50% of independent directors sit on three or more boards, and zero otherwise. All interaction variables are mean-centered. All control variables from previous analyses (i.e., Table 3) are included. Regressions include year and industry (Fama-French 48 classification) fixed effects and standard errors clustered by firm. Numbers in parentheses are t-statistics. Two-tailed statistical significance is indicated by ***, **, and * for 1%, 5%, and 10%, respectively.

Appendix A Part One: Variable definitions

Dependent variables	***Variable definitions***
CSP score =	sum of net score (total strengths – total concerns) from each of the six MSCI ESG STATS dimensions (community, diversity, employee relations, environment, human rights, product);
CSP strengths =	sum of total strengths from the six MSCI ESG STATS dimensions;
CSP concerns =	sum of total concerns from the six MSCI ESG STATS dimensions;
Community strengths =	sum of strengths from community and human rights dimensions;
Community concerns =	sum of concerns from community and human rights dimensions;
Employee strengths =	sum of strengths from employee relations and diversity dimensions;
Employee concerns =	sum of concerns from employee relations and diversity dimensions;
Environment strengths =	sum of strengths from environment dimension;
Environment concerns =	sum of concerns from environment dimension;
Consumer and supplier strengths =	sum of strengths from product dimension;
Consumer and supplier concerns =	sum of concerns from product dimension;
Test variables	
Committee =	indicator variable equal to one if a board-level committee focusing on sustainability related issues exists in firm-year;
Community focus =	indicator variable equal to one if a board-level committee focusing on community and/or human rights related issues exists in firm-year;
No community focus =	indicator variable equal to one if a board-level committee exists in firm-year and does not focus on community and/or human rights related issues;
Employee focus =	indicator variable equal to one if a board-level committee focusing on employee related issues exists in firm-year;
No employee focus =	indicator variable equal to one if a board-level committee exists in firm-year and does not focus on employee related issues;
Environment focus =	indicator variable equal to one if a board-level committee focusing on environment related issues exists in firm-year;
No environment focus =	indicator variable equal to one if a board-level committee exists in firm-year and does not focus on environment related issues;
Consumer and supplier focus =	indicator variable equal to one if a board-level committee focusing on product related issues exists in firm-year;
No consumer and supplier focus =	indicator variable equal to one if a board-level committee exists in firm-year and does not focus product related issues;
Committee size =	number of members on the committee;
Fully independent =	indicator variable equal to one if all members of the committee are independent directors;
Meeting frequency =	number of committee meetings;

Appendix A (continued)

Control variables

Board size =	natural log of number of members on the board of directors;
Independence =	percentage of directors who are independent;
Tenure =	mean tenure of all directors;
Busy board =	indicator variable equal to one if 50% or more of board members sit on at least three boards (including the associated company);
Size =	natural log of total assets at end of year;
Quick =	current assets divided by current liabilities;
ROA =	income before extraordinary items divided by total assets at beginning of the year;
Leverage =	long-term debt divided by total assets from end of year;
R&D investment =	ratio of research and development expense to sales

Appendix B Part One: Sustainability committee classification

Stakeholder groups	*MSCI dimension*	*Sample committee names (from coded data)*	*Common committee responsibilities*
Community	Community	Public interest, public issues, community and external relations, civic and charitable affairs, charitable contributions, etc.	Charitable giving, Community impact, Community engagement, volunteer programs, etc.
	Human rights	Public policy, public issues, corporate social responsibility, ethics compliance and sustainability, etc.	Labor rights, Human rights policies and initiatives, human rights violations, etc.
Employees	Employee relations	Occupational safety and environmental protection, operational safety, public policy, employee development and retention, etc.	Union relations, employee involvement, employee health and safety, professional development, child labor, etc.
	Diversity	Employee and public responsibility, public affairs, diversity review, corporate responsibility, excellence, etc.	Women and minority contracting, employment of the disabled, employment of underrepresented groups, etc.
Environment	Environment	Environmental health safety and public policy, environmental and safety, environmental and corporate responsibility, etc.	Waste management, climate change, water stress, biodiversity and land use, raw material sourcing, etc.
Consumer/supplier	Product	Environmental and safety, quality, public policy, best practices, nuclear, clinical quality, excellence, safety, etc.	Product quality and safety, customer relations, etc.

Appendix C Part One: Independent variable coding

The following responsibility statements are taken from the proxy filing for each committee-firm-year:

Arch Coal Inc. 2013
"Energy and Environmental Policy" Committee
The Energy and Environmental Policy Committee reviews, assesses and provides advice to the Board on current and emerging energy and environmental policy trends and developments that affect or could affect us. In addition, the Energy and Environmental Policy Committee makes recommendations concerning whether, and to what extent, we should become involved in current and emerging energy and environmental policy issues.

Delta Air Lines Inc. 2013
"Safety and Security" Committee

Among other matters, the Committee:

- oversees and consults with management regarding customer, employee and aircraft operating safety and security, including related goals, performance and initiatives by:
- reviewing current and proposed safety and security-related programs, policies and compliance matters
- reviewing matters with a material effect on Delta's flight safety operations and security
- establishing and approving annual safety and security goals
- reviewing the safety and security programs and performance of the Delta Connection carriers
- reviewing the security of the Company's information technology systems and operations, including defenses against cyber threats to the airline.

These descriptions illustrate that the committees focus on different dimensions of sustainability. These committees are therefore coded as one for the following indicators, which are used in empirical analysis.

Arch Coal Inc. 2013
"Energy and Environmental Policy" Committee
Committee
Environment focus
No community focus
No employee focus
No consumer/supplier focus

Delta Air Lines Inc. 2013
"Safety and Security" Committee

Committee
Employee focus
Consumer/supplier focus
No community focus
No environment focus

Appendix D Part Two: RepRisk Data: ESG issues examined

ENVIRONMENT	**SOCIAL**		**GOVERNANCE**
Environmental footprint	**Community relations**	**Employee relations**	**Corporate governance**
Global pollution • Climate change • GHG emissions	Human rights abuses and corporate complicity	Forced labor	Corruption, bribery, extortion, money laundering
Local pollution	Impacts on communities	Child labor	Executive compensation
Impacts on ecosystems and landscapes	Local participation issues	Freedom of association and collective bargaining	Misleading communication (e.g. "greenwashing")
Overuse and wasting of resources	Social discrimination	Discrimination in employment	Fraud
Waste issues		Health and safety issues	Tax evasion
Animal mistreatment		Poor employment conditions	Tax optimization
Controversial products and services			Anti-competitive practices
Product-related health and environmental issues			
Violation of international standards			
Violation of national legislation			
Supply chain			

Appendix E Part Two: Variable definitions

Risk measures	***Variable definitions***
NEG_MEDIA	Maximum of index measuring client negative media coverage of ESG practices during the audit negotiation period (fourth quarter of *t*-1 and first quarter of *t*), adjusted by negotiation period mean [RepRisk]
E_ISSUE	=1 if an environmental issue is covered, zero otherwise [RepRisk]
S_ISSUE	=1 if a social issue is covered, zero otherwise [RepRisk]
G_ISSUE	=1 if a governance issue is covered, zero otherwise [RepRisk]
Auditor response	
AUDITORCHANGE	=1 for companies that have an auditor change, zero otherwise [Audit Analytics]
RESIGN	=1 for companies that have an auditor resignation, zero otherwise [Audit Analytics]
LOGAUDITFEES	Natural logarithm of audit fees [Audit Analytics]
Control variables	
LNASSETS	Natural log of total assets [Compustat]
ROA	The ratio of net income to total assets (NI/AT) [Compustat]
LEVERAGE	The ratio of total liabilities to total assets (DLC+DLTT/AT) [Compustat]
SALESGROWTH	The ratio of the change in sales revenue to prior year sales revenue [Compustat]
ZSCORE	Calculated as the decile rank of the Altman's [1980] z-score for non-financial firms [Compustat]
MA	=1 if the company has a merger or acquisition, zero otherwise [Compustat]
FOREIGN	=1 if the company has foreign operations, zero otherwise [Compustat]
P_SCORE	Predicted probability of misstatement estimated using the Dechow et al. (2011) model as presented in Lobo and Zhao (2013)
RESTATEMENT	=1 for companies that announce a restatement to their financial reports, zero otherwise [Audit Analytics]
GC	=1 if the company received a going-concern modified audit opinion, zero otherwise [Audit Analytics]
INDUSTRYEXP	=1 if the listed auditor receives more than 30 percent of total audit fees in the associated 2-digit SIC code, zero otherwise [Audit Analytics]
FYE_DEC	=1 if fiscal year end in December, zero otherwise
SEGMENTS	The number of unique business segments
MW	=1 for companies disclosing a material weakness in their SOX section 302/404, zero otherwise [Audit Analytics]
Supplemental variables	
NEGMEDIA_PEAK_PRIOR	=1 if the index within the first through third quarters of t-1 is above the 60th percentile and if the index within the fourth quarter of t-1 and throughout year t is below the 40th percentile, zero otherwise [RepRisk]
NEGMEDIA_PEAK_NEGOT	=1 if the index within the fourth quarter of t-1 and the first quarter of t is above the 60th percentile and if the index within the second through fourth quarters of year t is below the 40th percentile, zero otherwise [RepRisk]
NEGMEDIA_PEAK_SUBSEQ	=1 if the index within the second through fourth quarters of year t is above the 60th percentile and if the index within the fourth quarter of t-1 and the first quarter of t is below the 40th percentile, zero otherwise [RepRisk]

Appendix E (continued)

BENFORD_SCORE	Maximum deviation of the cumulative differences between the distribution of leading digits in annual financial statement data and their theoretical Benford distribution, following Amiram et al. (2015) [Compustat]
BENFORD_FAIL	=1 if *BENFORD_SCORE* is significantly different than the critical value (equal to 1.36 divided by the square root of the total number of digits used) at the five percent level, zero otherwise [Compustat]
ABFEE	Difference between the actual and fitted values of audit fees estimated as a function of misstatement risk and other control variables (following the model in Lobo and Zhao (2013))
NEW_GC	=1 if *GC* is equal to one but was not in the prior year, zero otherwise [Audit Analytics]
MISSTATEMENT	=1 for companies where the financial reports contained a significant misstatement that subsequently led to a restatement, zero otherwise [Audit Analytics]
DACC	Discretionary accruals calculated using the modified Jones model with control for firm performance [Compustat]
TACC	The absolute value of abnormal accruals derived from the difference between total accruals (calculated as IB-OANC) and expected accruals estimated with the modified Jones model augmented with lag ROA (Kothari et al. (2005)) [Compustat]
DELAY_ADJ	The number of days between the fiscal year end date and the audit report date minus the SEC's filing deadline requirement (60, 75, and 90 days for large accelerated, accelerated, and non-accelerated, respectively) [Audit Analytics]
OANCF	Net operating cash flow [Compustat]
BIG4	=1 if Big 4 auditor conducts annual financial statement auit, zero otherwise [Audit Analytics]
STDOPCASH_5YR	The standard deviation of cash flows from operations calculated over five years with a minimum of three years [Compustat data OANCF]
STDSALES_5YR	The standard deviation of sales calculated over five years with a minimum of three years [Compustat data SALE]
FIRM_AGE	The number of years since formation
LITRISK	=1 for companies within 4-digit SIC codes from 3600 to 3675, zero otherwise
DISTRESSSED	=1 for companies with negative net income or net operating cash flows, zero otherwise
LOWHIGH_SUM	Number of individual issues (as listed in Appendix D) that move from a low reach media source in *t*-1 to a high reach media source in *t* [RepRisk]
LOWHIGH_SUM_LEAD	Number of individual issues (as listed in Appendix D) that move from a low reach media source in *t* to a high reach media source in *t*+1 [RepRisk]

Appendix F Part Three: Variable definitions

Test variable	***Variable definition***
NEG_MEDIA	Maximum of index measuring negative media coverage of ESG practices within the twelve months prior to the CEO turnover date for firm-year observations with a CEO dismissal, and within the fiscal year for firm-year observations without a CEO dismissal [RepRisk]
E_ISSUE	=1 if an environmental issue is covered within the twelve months prior to the CEO turnover date for firm-year observations with a CEO dismissal, and within the fiscal year for firm-year observations without a CEO dismissal, zero otherwise [RepRisk]
S_ISSUE	=1 if a social issue is covered within the twelve months prior to the CEO turnover date for firm-year observations with a CEO dismissal, and within the fiscal year for firm-year observations without a CEO dismissal, zero otherwise [RepRisk]
G_ISSUE	=1 if a governance issue is covered within the twelve months prior to the CEO turnover date for firm-year observations with a CEO dismissal, and within the fiscal year for firm-year observations without a CEO dismissal, zero otherwise [RepRisk]
HIGH_REACH	=1 if the firm-year observation was equal to one for the associated issue indicator variable and an issue within that category was covered by a high reach media source (e.g., Wall Street Journal, New York Times, etc.), zero otherwise [RepRisk]
LOW_REACH	=1 if the firm-year observation was equal to one for the associated issue indicator variable and no issues within that category were covered by a high reach media source (e.g., Wall Street Journal, New York Times, etc.), zero otherwise [RepRisk]
HIGH_SEV	=1 if the firm-year observation was equal to one for the associated issue indicator variable and an issue within that category was classified as high severity, zero otherwise [RepRisk]
LOW_SEV	=1 if the firm-year observation was equal to one for the associated issue indicator variable and no issues within that category were classified as high severity, zero otherwise [RepRisk]
HIGHSEV_HIGHREACH	=1 if the firm-year observation was equal to one for both *HIGH_SEV* and *HIGH_REACH*, zero otherwise
LOWSEV_HIGHREACH	=1 if the firm-year observation was equal to zero for *HIGHSEV_HIGHREACH* and equal to one for both *LOW_SEV* and *HIGH_REACH*, zero otherwise
HIGHSEV_LOWREACH	=1 if the firm-year observation was equal to zero for both *HIGHSEV_HIGHREACH* and *LOWSEV_HIGHREACH* and equal to one for both *HIGH_SEV* and *LOW_REACH*, zero otherwise
LOWSEV_LOWREACH	=1 if the firm-year observation was equal to zero for *HIGHSEV_HIGHREACH, LOWSEV_HIGHREACH*, and *HIGHSEV_LOWREACH* and equal to one for both *LOW_SEV* and *LOW_REACH*, zero otherwise
Dependent Variables	
CEO_DISMISSAL	=1 for companies that have a CEO dismissal, zero otherwise [Audit Analytics D&O changes]
INTERNAL_CEO	=1 for companies with a replacement CEO that was employed with the firm more than one year before the turnover announcement, zero otherwise [BoardEx]
EXTERNAL_CEO	=1 for companies with a replacement CEO that joined the firm less than one year before the turnover announcement, zero otherwise [BoardEx]

Appendix F (continued)

Control variables

ROA	The ratio of net income to total assets (NI/AT) [Compustat]
STOCKRETURN	Buy-and-hold abnormal return (BHAR) for the twelve months ending at FYE [Compustat]
CEO_AGE	Age of the former CEO [BoardEx]
LNASSETS	Natural log of total assets [Compustat data AT]
SEGMENTS	The number of business segments
BOARD_INDEP	Percent of directors who are unaffiliated with the firm beyond their directorship [BoardEx]
BOARD_SIZE	Number of directors on the board [BoardEx]
COMMITTEE	=1 if a board-level committee focusing on sustainability-related issues exists, zero otherwise
BOARD_BUSY	=1 if more than 50 percent of independent directors are busy, which is defined as serving on three or more boards, zero otherwise
RESTATEMENT	=1 for companies that announce a restatement to their financial reports, zero otherwise [Audit Analytics]
MW	=1 for companies disclosing a material weakness in their SOX section 302/404, zero otherwise [Audit Analytics]
TALENT	=1 for companies with at least one executive with outside directorships, zero otherwise[BoardEx]
HEIR_APPARENT	=1 for companies with a non-CEO president or COO who has been in their position for less than two years before the turnover announcement, zero otherwise [BoardEx]

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