

Former CEO Directors: Lingering CEOs or Valuable Resources as Comeback CEOs?

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Abstract

A CEO is more likely to remain on the board of directors of his firm after retirement the better is the firm's market and industry-adjusted performance, the longer is the CEO's tenure, and if the CEO is a founder of the firm. These former CEOs continue to have an impact on their firms. The tenure of their successors is shorter. After extremely poor firm performance under their successors, they frequently come out of retirement and return to the CEO position. When they do so, their firms do as well as industry and past performance matched firms. However, there are potential costs of retaining a former CEO as a board member. Former CEOs are more reluctant to agree to changes in corporate policies. Furthermore, former CEOs may undermine the authority of their successor. When a former CEO was rehired and steps down for the second time, an external CEO tends to only accept the appointment if the former CEO resigns from the board so that a clean transfer of power is assured.

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Q. After 23 years as CEO, you resigned in July 2000. Four months later, your replacement, ex-AT&T executive David Grimes, was gone, and you were CEO again. What went wrong?

John Sykes, 66, founder, chairman, CEO and president of Sykes Enterprises Inc.: “*David Grimes is a very capable person, has a great track record. [...] But he came in with a tremendous handicap. And that handicap was that I sat here as chairman. No matter whether I moved out of this office and went down to the 28th floor, my shadow was here. [...] It is very difficult for anyone from the outside to come into a company where the entrepreneur is still there and expect that they can come in and make the changes that are necessary.*”

St. Petersburg Times, January 6, 2003

1. Introduction

Chief executive officers (CEOs) are central figures of corporations, making decisions that have major valuation consequences for their firms’ shareholders. Consequently, one of the most important decisions of the board of directors is the CEO hiring decision. Although a board may have carefully selected a CEO candidate who has the potential to maximize shareholder value, there is some residual uncertainty about his ability. It, therefore, may be valuable for a firm to retain the former CEO on the board because he could help evaluate his successor and, if the successor was not capable of running the firm, come back to his old position. However, a potential cost of retaining a former CEO as a board member is that he may be more reluctant to agree to necessary changes in corporate policies or that he undermines the authority of a new CEO.

Brickley, Linck, and Coles (1999) study the *determinants* of the board membership of former CEOs. They report that 50% of former CEOs sit on their own board two years after retirement, and that obtaining the board membership is positively related to market- and industry-adjusted stock performance and to the tenure of the former CEO. We contribute to the literature by examining the *consequences* of having a former CEO as a board member.

We use a sample of 641 turnovers at publicly traded US firms for the period from 1993 to 2005 to study whether former CEOs are valuable resources or represent a cost to their firms. Similar to Brickley, Linck, and Coles (1999), we find that the tenure of the first CEO, the market- and industry-adjusted stock market performance, and the founder-status of the CEO are strong predictors of a former CEO's board membership one year or two years after his retirement.

We use two tests to study whether retaining a former CEO on the board has consequences for managerial hiring decisions. First, we estimate Cox proportional hazard models to determine whether the presence of the former CEO on the board has an impact on the tenure of his successor. It may be valuable to have a former CEO on the board because he can help evaluate his successor. A former CEO may recognize sooner than other board members that his successor lacks ability and encourage a new executive search. On the other hand, a former CEO may convince a board to give a CEO more time to improve performance because he believes the poor performance is the result of bad luck and not managerial skill. We find that the board membership of the former CEO has a significantly negative impact on the tenure of the successor CEO, carefully controlling for industry-adjusted performance of the successor CEO and other determinants of turnover. The relative risk of a CEO to lose his job is 40% higher when the former CEO is still a director.

Second, we analyze actual rehiring decisions. While several recent rehire decisions have triggered considerable media interest (e.g., Michael Dell, Charles Schwab, and Paul Allaire at Xerox), very little is known about how often and under what circumstances such an event happens.¹ If the labor market for CEOs is characterized by scarcity of supply, it may be valuable

¹ e.g., Anonymous (2001), Darlin and Lohr (2007), Lublin and White (2007), Jones (2006), and Olian (2003). To the best of our knowledge, no academic paper has dealt with the phenomenon.

to retain a former executive on the board of directors to have a potential CEO candidate available.² Such an option may be especially valuable if a large amount of firm-specific knowledge is necessary to run the firm or if the firm faces higher uncertainty. We find that rehiring a former CEO is not an uncommon event. Approximately 10% of our sample firms rehire their former CEOs. The typical rehired CEO comes back after two years in retirement, is 61 years old at the time of his reappointment, and stays on as CEO for another two and a half years. Having controlled for the former CEO remaining on the board, a firm is more likely to rehire the former CEO if the former CEO is the chairman of the board, if the former CEO has not been in retirement for too long, if the current CEO is an internal appointment, and if the firm has particularly bad stock performance under the current CEO. One interpretation of this result is that it is especially valuable to retain a former CEO for a short time because he is willing to come out of retirement to run the firm again after a sudden negative shock to firm performance for which his hand-picked successor is potentially responsible.

The market reacts negatively to the rehiring of the former CEO. The industry- and market-adjusted cumulative abnormal announcement returns for the three-day event window around the rehiring announcement are -3.9% and -3.6%, respectively, and significant at less than the five percent level. Denis and Denis (1995) and Warner, Watts, and Wruck (1988) suggest that the cumulative return has an information component that is generated by the signal that the turnover announcement conveyed information about the firm's worse than expected performance and a real component that is generated by the market's assessment about the quality of the new CEO. Thus, the three day cumulative return could be contradictory to our conjecture that having the former CEO on the board so that he can return as CEO is valuable.

² Several recent papers suggest a limited supply of strong CEO candidates (e.g., Himmelberg and Hubbard (2000), Gabaix and Landier (2006), and Rajgopal, Shevlin, and Zamora (2006))

We perform additional tests to determine if the real component is driving the negative announcement returns. These tests show that the market did not react positively at the first retirement of the comeback CEO and that the CEO appears to perform as well as a CEO of a different firm from the same industry. Thus, the real component does not seem to be driving the negative announcement returns. Overall, one interpretation of the announcement return evidence is that the market learns that no outside or other internal candidate was available or willing to become CEO. Nevertheless, the board decided to remove the current CEO. The announcement of this decision lead to a re-assessment of the firm's viability.

The quote at the beginning of the article indicates a potential cost of having a strong former CEO sitting on the board of directors, because a new CEO cannot make the necessary changes to improve or maintain performance as his suggestions are blocked or undermined in board meetings.³ In many succession cases in which the former CEO stays on the board, the successor was an internal candidate who was likely groomed and selected by the former CEO, which may amplify these problems. Also, a survey of 1,000 directors conducted by the magazine *Corporate Board Member* in conjunction with *Price Waterhouse Coopers* in 2003, found that only 25.3% of survey respondents said that it was a good idea to have the former CEO on the board.

We perform two analyses to study whether it is a case of a fundamental misjudgment of the talent of the internal candidate or whether the former CEO could be partially responsible for the current CEO's problems by maintaining a strong presence within the firm and interfering with the decisions the new CEO makes. First, we analyze changes in the investment policies in firms with and without the former CEO as a director. Second, we look at the incidence of

³ Guembel and Casamatta (2006) show theoretically how such legacy considerations of a CEO interact with strategy changes and CEO turnover.

internal versus external hires at the second retirement of the rehired CEO. We find that corporate policies such as capital expenditures, tangible assets, research and development expenditures, and acquisition activity are more constant across a turnover when the former CEO continues on the board of directors. One interpretation of this result is that the new CEO may be more limited in his impact on a firm's investment decisions when the former CEO is still present.

In 38 cases, the rehired former CEO retires for a second time. In a majority of these cases, the new CEO is an external candidate and a smaller fraction of rehired former CEOs remain on the board. The negative correlation between an external CEO and the former CEO remaining on the board is consistent with the idea that an external CEO tends to only accept the appointment if the powerful former CEO resigns from the board so that a clean transfer of power is assured.

Overall, our evidence is consistent with former CEOs as directors having a continuing impact on their firms' decisions. The tenure of their successor is shorter if the former CEO is present on the board, and in firms with rapidly deteriorating performance and the need to change CEOs quickly, former CEOs are willing to come back to run the firm again. But there also appears to be a cost associated with the retention of the former CEO, as corporate policies are more correlated across CEO in firms with former CEOs on the board suggesting that it is more difficult to implement changes in firms with former CEOs on the board.

The remainder of the paper is organized as follows. Section 2 describes the sample. Section 3 develops hypotheses about the consequences of the decision to retain the former CEO on the board of directors. The empirical results are discussed in Section 4. Section 5 concludes.

2. Data and Sample Description

We use data from four different sources. We obtain our initial sample of CEO turnovers from the ExecuComp database. Compustat provides data on accounting variables, CRSP data on returns, and CompactDisclosure data on the board of directors. For some of our empirical tests, we require the identity of the previous CEO to verify whether he continues on the board of directors until the turnover of his successor. Therefore, our focus is, for each firm in Execucomp, on firms that have reported at least two turnovers in the period 1992 to 2004. This requirement leads to a sample in which the tenure of the CEO tends to be shorter than the average, unconditional tenure of seven years (e.g., Kaplan and Minton (2006)) and thus a sample in which involuntary turnovers are more frequent. There are 810 such turnover events in Execucomp.

Next, we exclude interim CEOs from our sample. We conjecture that a tenure of less than six months indicates that a CEO was an interim CEO. Changing the minimum tenure requirement to three months or twelve months does not change our results. After imposing a tenure of at least six months, our sample contains 641 turnover events.

For each CEO turnover in our sample, we match the name of the prior CEO to the list of directors obtained from the monthly CompactDisclosure compact discs and verify whether the prior CEO was a nominee for a director position one year and two years after retirement and at the proxy date preceding the turnover of his successor.⁴

To identify whether a previous CEO was rehired, we search whether the name of an executive appears twice in the time-series of CEOs on ExecuComp. For each of these instances,

⁴ For firms in which we are unable to match CEOs to the director list from CompactDisclosure, we manually check the proxy statements to identify whether the former CEO was sitting on the board of directors at the turnover of his successor.

we verify that the previous CEO was indeed rehired, and that it is not a coding mistake (e.g., there are several cases of an alternate reporting of co-CEOs). We identify 88 events in our sample of firms which qualify as a rehiring decision. Later on, one of our tests examines under what circumstances a firm rehires their former CEO. Such a test requires that the former CEO was indeed available to be rehired. We assume that every former CEO who is a board member at the turnover of his successor is available to be rehired.⁵ This requirement discards twelve rehiring events from our sample. We are understating the pool of available former CEOs, as a retired CEO may choose to leave the board of directors at retirement, yet still be able and willing to come back to his former employer. However, to include these CEOs in our study, we would have to make more subjective assessments about availability of former CEOs (e.g., is a former CEO who stepped down due to health issues available or not?), which appears undesirable.

One obvious concern regarding rehired CEOs is whether they merely come back as an interim CEO while the firm is conducting an executive search. We address this issue by implementing a six-month tenure requirement to qualify as a rehired CEO.⁶

Table 1 tabulates the number of overall turnovers and statistics related to the board service of former CEOs. The second and third columns report the number of former CEOs who are director for at least one and two years, respectively. There does not appear any obvious time trend, and the fraction of 43.1% of former CEOs who are director two years into retirement is close to the number of 50% reported by Brickley, Coles, and Linck (1999). The fourth column shows the number of turnovers in which the former CEO sat on the board of directors at the time

⁵ Theoretically, a former CEO could remain on the board of his own firm, but move on to become an executive at a different firm. However, even the unconditional probability of stepping down as a CEO and becoming an executive at a different firm is very low. Gibbons and Murphy (1992) estimate it to be 2.2%, and Brickley, Linck, and Coles (1999) estimate it to be 3.2%.

⁶ An alternative approach is to search all announcements and the first annual report after the reappointment for the words interim or temporary in connection with the rehired CEO. The weakness of this approach is that a CEO may originally intend to stay as an interim CEO, but then continue in office for many years. Yet, our results do not change when we use this criterion to clean our sample.

of the turnover, and the fifth column lists the number of turnovers to the former CEO. From 1996 to 2003, we observe 205 turnovers where the former CEO still sat on the board at the time of the turnover and 67 turnovers to former CEOs, without an obvious time trend. Overall, the fraction of turnovers in which the former CEO still sat on the board is 32%, while the unconditional probability of rehiring the former CEO is 10.5% (67/641). These numbers appear to be higher than commonly thought (e.g., Anonymous (2001)).

[Insert table 1 here]

We will frequently refer to three groups of CEOs when describing our empirical tests. The three groups are the former CEO, current CEO, and successor CEO. The former CEO is the CEO that is in office before the current CEO, who is in turn succeeded by the successor CEO. For the sample of rehired CEOs, the former CEO and the successor CEO are identical: it is the rehired CEO. For the sample in which the former CEO is not hired, the former, current, and successor CEO are three different individuals.

Table 2 reports CEO characteristics for the three different CEOs, split by whether the former CEO is director at the time of turnover of the current CEO.

[Insert table 2 here]

For the sample in which the former CEO is on the board until the turnover of his successor (i.e., the current CEO), the former CEO is a founder of the company 30% of the time, has an average first tenure of 10.6 years, owns 5% of the firm's stock when he first left the CEO

position, and has an annualized excess return of 5% during his tenure. These numbers are statistically greater than those for the sample of former CEOs who do not remain on the board. In this sample, the former CEO is a founder 10% of the time, has an average tenure of 7.6 years, own 2% of the firm's outstanding stock at retirement and has an annualized excess return of -8% during his tenure.

The average age and tenure of the current CEO in the sample in which the former CEO stays on the board is significantly lower than those of the current CEO in the firms in which the CEO does not stay on the board. Additionally, the excess return in the last year of the current CEO's tenure is significantly lower in the sample where the former CEO stays on the board. There is no statistical difference in the classification of the current CEO as an insider or outsider between the two groups; most current CEOs are insiders.

3. Relevant Literature and Testable Hypotheses

In this section, we discuss the determinants of the decision to retain the former CEO on the board of directors and relate them to prior literature. We then develop hypotheses about the *consequences* of retaining the former CEO on the board.

3.1. Determinants of the retention decision

Brickley, Linck, and Coles (1999) argue that managers will have career concerns even in the final years of employment as long as managers care about post-retirement opportunities and that these opportunities are positively correlated with the manager's performance during the final years of his tenure. They test this hypothesis during the 1989 to 1993 period by examining the likelihood that a retiring CEO serves on his own and other boards after retirement. They find

that the likelihood of a CEO remaining on his own board two years after retirement is positively related to his firm's stock performance while CEO, while the likelihood of serving on other boards is positively related to accounting performance. Given these results, we control for a firm's stock performance during the former CEO's tenure in our empirical tests examining the likelihood that a CEO stays on the board after retirement.

Several recent papers have argued that the supply side of the market for CEOs is relatively scarce (Himmelberg and Hubbard (2000), Gabaix and Landier (2006), and Rajgopal, Shevlin, and Zamora (2006)). These arguments imply that firm-specific characteristics that measure the scarcity of the supply of CEOs and the complexity of the organization should be significant determinants of the decision to retain a former CEO on the board.

The costs of transferring firm-specific knowledge is an important consideration in the process of CEO turnover (see, e.g., Vancil (1987) and Naveen (2006)). We would expect that the likelihood of retaining the former CEO as a board member will be higher in firms with more firm-specific capital. We measure firm-specific capital using the ratio of research and development expenditures to sales, the ratio of net property, plant and equipment (PPE) to total assets, and a high tech industry indicator variable following Loughran and Ritter (2004). We also include firm size, measured by the natural logarithm of total assets as an additional proxy for firm complexity.

CEO specific characteristics potentially are important determinants of the retention decision, but it is less clear whether these characteristics are proxies for the desire of the board to retain a high quality CEO or if these characteristics are proxies for the power and entrenchment of a former CEO who can impose his will to remain on the board. For example, we include the tenure and founder status of the prior CEO. These attributes could measure the quality of the

CEO. As a CEO spends more time in the office, he accumulates more knowledge about the firm and industry, and founders know their business very well. On the other hand, a long prior tenure and founder status also are good measures of power and potential entrenchment.⁷

3.2. Consequences of a former CEO on the board

3.2.1. Length of tenure of successor CEO

It may be valuable to have a former CEO on the board because he can help evaluate his successor. Several papers have argued that CEOs are sometimes paid for luck, which suggests that it may be difficult to separate skill and luck in managerial decisions (e.g., Daines, Nair, and Kornhauser (2005), and Bertrand and Mullainathan (2001)). A former CEO may have the ability to assess the current CEO and possibly convince the board to give the current CEO more time to improve performance because he believes the poor performance is the result of bad luck and not managerial skill. In this case, we would expect the tenure of the success CEO to be longer if the former CEO is on the board. In contrast, if the former CEO is acting in the best interests of shareholders and is better able to more quickly identify a poorly performing successor, because he knows the business very well, we would expect the dismissal of the current CEO and shorter tenure.

Given the extant research on CEO turnover, we also expect the tenure of the successor CEO to be related to performance and CEO age.⁸ We control for these attributes in our

⁷ Adams, Almeida, and Ferreira (2005) include an indicator variable for founder status as a proxy for CEO power. Consistent with the management literature (Donaldson and Lorch (1983) and Finkelstein (1992)), Adams, Almeida, and Ferreira (2005) and Fahlenbrach (2006) consider CEOs who also are founders to be more influential, and show that they perform better.

⁸ Prior literature on CEO turnover has documented that there is a negative association of CEO turnover with performance (see, for example, Warner, Watts, and Wruck (1988), Huson, Parrino, and Starks (2001), Jenter and Kanaan (2006), and Kaplan and Minton (2006)).

regressions. We also control for industry structure by including the measure of industry homogeneity of Parrino (1997) and an indicator variable for high tech industries.

3.2.2. Decision to rehire the former CEO

Parrino (1997) shows that the availability of a strong CEO candidate is an important consideration in the decision to replace a poorly performing CEO. For example, exceptionally poor firm performance under the current CEO may trigger the need for an unanticipated quick turnover without adequate time for succession planning. A firm may be more willing to initiate a search process if a viable alternative solution to the problem exists – the availability of its former CEO who still sits on the board of the firm. Additionally, if the labor market for CEOs is characterized by scarce supply, then firms with former CEOs on the board may be quicker to exercise the option to rehire a former CEO. This option is more likely to be exercised the lower is firm performance under the current CEO. We look at the actual incidences of the former CEO coming back to the CEO position to shed light on what drives rehiring decisions. Note that it is important to account for sample selection in the rehiring regressions, because it is likely that only certain types of CEOs stay on their old firms' boards, and that the characteristics that determine the decision to stay on the board are correlated with the characteristics that drive the decision to come back to run the firm again. We use the procedure suggested by Heckman (1974) to account for such a sample selection bias.

3.2.3. Implementation of changes in corporate policies

Weisbach (1995) documents that CEO changes that are initiated by the board and normal retirement both lead to divestitures of poorly performing assets. He concludes that these results

suggest that CEO turnover is important because it is part of the process of reversing managerial motivated acquisitions. Weisbach, however, does not control for whether the former CEO stays on the board. One potential cost of the CEO staying on the board is they there may be no implementation of such necessary changes. In a similar spirit, Guembel and Casamatta (2006) suggest that CEOs with legacies – long-term projects with cash flows that are difficult to change – can have an impact on turnover decisions.

Finally, the potential cost of retaining a strong former CEO-director has also been noted by the business press. For example, a 2003 *Business Week* article raised concerns about having retiring CEO Sanford Weill on the board after retirement.⁹ As pointed out in the article, the new CEO (Charles Prince III) may be undermined by the former CEO who is a board member and in a powerful position to “*cramp Prince’s style*”, i.e. to question new strategies suggested by the new CEO.

We examine changes in corporate policies in firms with and without the former CEO as a director. If the former CEO on the board has a strong presence we expect that corporate policies under the former CEO and the current CEO be more correlated when the CEO remains on the board.

3.2.4. *External hires and strong former CEO-directors*

Another potential cost of having a former CEO on the board is the reluctance of an external hire to join the firm. The quote by John Sykes at the beginning of the paper is suggestive of this view. We examine the incidence of external hires as new CEOs at the time of the former CEO’s retirement and at the time of rehired CEO’s second retirement. If this

⁹ See Lavelle (2003).

reluctance on the part of potential external hires exists, we expect to see more internal hires in firms where the former CEO stays on the board.

4. Empirical results

4.1. Determinants of the decision to retain the former CEO as board member

[Insert table 3 here]

Table 3 presents descriptive statistics on firm characteristics for the sample of firms where the former CEO stays on as a director and the sample where the former CEO does not stay on the board. The last column of Table 3 reports the p-values for the differences in means and medians between the two groups. The accounting variables are taken from the last 10-K available prior to the turnover of the current CEO.

Firms where the former CEO stays on the board have better growth opportunities than firms where the former CEO does not stay on the board, as evidenced by the significantly higher median market-to-book ratios and sales growth. The two groups of firms also are different with respect to firm size, market leverage, dividends, and return on assets. The firm size, market leverage and dividend level of firms where the former CEO stays on the board are significantly lower than those of firms where the CEO does not stay on the board. In contrast, the former group of firms has significantly higher returns on asset than the latter group of firms. The two groups of firms are not statistically different with respect to capital expenditures, net PPE, R&D expenditures, dividend payer status, high tech classification, and a measure of industry homogeneity.

Overall, the univariate statistics of Tables 2 and 3 show that there are stock market performance differences between firms with and without former CEOs on the board and some differences in firm characteristics. The firms with former CEOs sitting on the board have better stock performance during the former CEO's tenure and worse stock market performance during the last year of the current CEO's tenure than firms without the former CEO on the board. Firms with former CEOs on the board also have better growth opportunities, are more profitable and have lower levels of leverage and dividends than firms without former CEOs on the board.

[Insert table 4 here]

In Table 4, we examine the probability that the CEO stays on the board of directors after his retirement. We estimate this probability at three different points: one year after retirement, two years after retirement and at the turnover of the current CEO. The dependent variable is equal to one if the former CEO sits on the board for at least one year after retirement (column 1), at least two years after retirement (column 2), or until the turnover of the current CEO (his successor) (column 3). The table reports marginal effects from a probit regression.

Consistent with the findings of Brickley, Linck and Coles (1999), the probability of remaining on the board at each horizon is positively and significantly related to the firm's stock performance over the former CEO's tenure. For example, a one standard deviation increase in the abnormal return increases the probability of the former CEO staying on the board for at least two years after retirement by about six percent. This is economically meaningful given the unconditional mean of a former CEO remaining on the board for at least two years is 43.1% (see

table 1). In contrast, accounting performance is not statistically related to the probability of a former CEO staying on the board after retirement.

CEO characteristics also are important determinants of the probability of a former CEO staying on the board. If a former CEO is a founder of the firm, the probability of his staying on the board for at least one year or two years after retirement increases by about 13%. Even larger, the probability that the former CEO is on the board at the time of his successor's turnover increases by 18.1% if the former CEO is the founder of the firm. The probability of the former CEO staying on the board also is higher for younger current CEOs. For example, a former CEO is 11% more likely to stay on the board for at least a year if the firm's current CEO is 10 years younger. Finally, the former CEO is more likely to stay on the board for at least one year and two years after retirement if his successor is an internal candidate. This is consistent with an internal succession process as described in Naveen (2006) or Vancil (1987), but also with the idea that external hires may be more reluctant to join the firm if a clean transfer of power is not assured.

4.2. Consequences of the former CEO staying on the board

In this section, we examine consequences of the decision to retain a former CEO on the board of directors. We examine the relation between a former CEO remaining on the board and the tenure of the current CEO (his successor) in section 4.2.1. In section 4.2.2, we examine the decision to rehire the former CEO. Potential costs of retaining a former CEO on the board are examined in sections 4.2.3 and 4.2.4.

4.2.1. Does CEO tenure depend on the former CEO's directorship?

[Insert table 5 here]

As previously discussed, a former CEO on the board may be better able to identify a poorly performing CEO and suggest the dismissal of the CEO. Alternatively, the former CEO on the board may convince a board to give his successor, especially if hand picked, more time to improve performance. In table 5, we report the results from a Cox proportional hazard model of the tenure of the current CEO (i.e., the successor to the former CEO). Each CEO's career is treated as a single observation. Since our sample construction requires a turnover of the current CEO, the Cox proportional hazard model is estimated with uncensored data; every observation has a failure event (i.e., the current CEO's employment contract is terminated). The dependent variable is the total months that the current CEO serves as CEO. The hazard ratios are reported in table 5. A coefficient larger than one indicates that an increase in the independent variable leads to an increase in the probability of failure (i.e., a decrease in CEO tenure).

Column one (base-case) includes all observations. The independent variables are measured at the time of the appointment of the current CEO. As shown in table 5, the tenure of the current CEO significantly increases if the current CEO is an internal hire, while the tenure significantly decreases for older CEOs. The coefficient estimate on current CEO age at appointment is statistically significant and greater than one. One potential explanation for the longer tenure of internal hires is that the board is more lenient with an internal, better known candidate than with a lesser known external candidate. CEO tenure also is related to the size of the firm: tenure increase as firm size increases. Finally, an increase in Parrino's (1997) measure

of industry homogeneity increases the tenure of the former CEO implying CEOs in more homogenous industries have longer tenures.

In the remaining regressions, we add stock performance variables and an indicator variable equal to one if the former CEO remains on the board one year after retirement (columns 2 and 3) or until the turnover of his successor (columns 4 and 5). In columns 2 and 4, we add a continuous measure of stock performance. In columns 3 and 5, we add an indicator variable equal to one if the stock return is in the bottom quartile.

As reported in Table 5, the coefficient estimates on the continuous stock performance variables are significantly less than one and those on the indicator variable for performance in the bottom quartile are significantly greater than one. These estimates indicate that poor stock performance significantly decreases the current CEO's tenure. This result is consistent with extant research on CEO turnover. The economic magnitudes appear large. For example, the relative risk of termination is 33% higher for a current CEO whose performance is in the bottom quartile.

Controlling for stock performance, the presence of the CEO on the board until the turnover of his successor decreases the tenure of the current CEO. This result is consistent with the idea that the former CEO can potentially spot a poorly performing CEO and move for his dismissal. The relative risk of a CEO to lose his job is 40% higher when the former CEO is still a director. In contrast, if the former CEO sits on the board for one year after retirement, the tenure of the successor CEO is marginally longer or not statistically changed.

4.2.2. *Decision to rehire former CEOs*

4.2.2.1. *When do former CEOs return to their firms?*

In Table 6, we examine the determinants of the decision to rehire the former CEO who sits on the board at the time of the current CEO's turnover. It is important to account for sample selection in the rehiring regressions. As shown in Table 4, only certain types of CEOs stay on the board after retirement and it is likely that the characteristics that determine the decision to stay on the board are correlated with the characteristics that drive the decision to come back to run the firm again. We use the two-stage selection model suggested by Heckman (1974) to account for such a sample selection bias. The first stage estimates the determinants of the probability that the former CEO stays on the board after retirement. The second stage models the likelihood that a firm rehires the former CEO given that the former CEO is on the board at the time of the current CEO's turnover. As shown in table 6, the Wald test of independence of selection and principal equation indicates that these decisions are related and that the Heckman selection model is the appropriate econometric model.

[Insert table 6]

The independent variables of the selection equation are those used in Table 4. Consequently, the former CEO is more likely to remain on the board of directors the better is the firm's stock performance during his tenure, the longer is his tenure, the smaller is the firm and if he is the founder of the firm.

The results in Table 6 show that, controlling for the likelihood that the CEO remains on the board, the probability of rehiring the CEO is significantly related to CEO characteristics and

firm characteristics. The marginal effect for the variable ‘former CEO years in retirement’ is negative and significant indicating that the longer the former CEO is in retirement the lower is the probability that he is rehired as CEO. The probability that the former CEO is rehired is 20.9% higher if the former CEO is chairman of the board at the time of the current CEO’s turnover. This marginal probability is significant at the one percent significance level. One interpretation of this result is that as chairman, the former CEO is in a powerful position to convince the board that he is the only viable candidate who can reverse the poor performance under the current CEO.

The probability of rehiring the former CEO also is significantly related to whether the current CEO was an internal hire and whether the stock performance of the current CEO is in the bottom quartile. A firm is 13.5% more likely to rehire the former CEO if the current CEO is an internal hire. This is interesting because presumably the internal CEO was hand picked by the current CEO. The fact that a firm then rehires its former CEO may indicate that no succession plan is in place and that the former CEO, knowing the business as well as the internal successor, is the only viable candidate.

Stock performance also is correlated with the likelihood of rehiring a former CEO. The probability that a firm will rehire a former CEO increases by 17.5% if the current CEO is a bottom quartile performer. While Denis and Denis (1995) and Warner, Watts, and Wruck (1988) document a positive relation between poor stock performance and an external hire, this finding suggest that for firms with particularly poor performance, the board hires an internal candidate – the former CEO.

While firm size is negatively related to the probability of the former CEO staying on the board, if the former CEO stays on the board the probability of rehiring the former CEO is

positively related to firm size. Finally, firms with no R&D expenditures reported are less likely to rehire the former CEO. If firms do not report R&D expenditures because they are small and grouped elsewhere, this finding is consistent with firms with more firm specific knowledge rehiring a former CEO.

Overall, in firms with rapidly deteriorating performance and the need for a quick turn around, the former CEO is rehired.

4.2.2.2. The market reaction to the rehiring decision

The upper graph of Figure 1 shows the mean industry-adjusted and market-adjusted cumulative returns in the 20-day event window around the announcement of the turnover of the current CEO. The market appears to react strongly negatively to the announcement of the decision to rehire the former CEO, with both industry- and market-adjusted returns of approximately minus four percent. In untabulated results, we show that both the industry-adjusted and market-adjusted cumulative abnormal announcement returns for the three-day event window [-1, 1] around the announcement of the re-appointment of the former CEO are -3.9% and -3.6%, respectively. These negative cumulative returns are statistically significantly different from zero at less than the five percent level.

Several studies have examined the stock market announcement returns to management turnover (e.g., Denis and Denis (1995), and Warner, Watts, and Wruck (1988)). Both Denis and Denis (1995) and Warner, Watts, and Wruck (1988) hypothesize that there could be at least two different components that form the cumulative abnormal announcement returns: an information component and a real component. The information component of the abnormal return is generated by the signal that the turnover announcement conveys about the worse than expected management performance and quality. The real component of the abnormal return is generated

by the market's assessment of the ability of the new CEO to improve performance. Hence, the negative announcement returns could be somewhat contradictory to our conjecture that having the former CEO on board is valuable. To see whether the real component possibly drives the announcement returns, we offer two tests.

We can observe the market's reaction to the *first* retirement of the comeback CEO. The lower graph of Figure 2 shows the mean industry-adjusted and market-adjusted cumulative returns around the announcement of the turnover of the comeback CEO during his *first* tenure. The market does not appear to react positively to the departure of the former CEO, which we would have expected if the strong negative reaction to his reappointment was driven by the real component.¹⁰

Second, we ask how the former CEO is performing by examining two measures of abnormal accounting performance, return on assets (ROA) and operating cash flow (OCF). We use an industry and performance matched benchmark, as suggested by Barber and Lyon (1996), Holthausen and Larcker (1996), and Larcker (2003) to detect any abnormal performance.¹¹ Barber and Lyon indicate that by matching sample firms to firms based on lagged performance, a researcher can control for firm characteristics such as corporate strategy, managerial ability, or the nature of investment opportunities, variables normally unobservable to the researcher.

The median abnormal ROA, calculated as described above, for the first year of the comeback CEO is 0.19%. The abnormal OCF for the first year of the comeback CEO is 0.79%.

¹⁰ We confirm in untabulated regressions that the cumulative abnormal returns over the (-1, +1)-day event window are not statistically different from zero.

¹¹ Barber and Lyon (1996) evaluate the empirical power and specification of nine accounting performance measures and an appropriate test to detect abnormal performance and find that a past-performance-matched benchmark is most appropriate and that a non-parametric Wilcoxon test is the most powerful test. Since we have a smaller sample of firms, we use the matched firm approach as described by Larcker (2003). For the first year of each comeback CEO, we find a matched firm from the same industry that had a similar performance in the previous fiscal year $t-1$ (the last year of the current CEO). We then calculate abnormal accounting performance in year t by deducting the ROA or OCF of the benchmark firm from the ROA or OCF of the comeback CEO's firm.

Both abnormal accounting performance measures are not statistically different from zero.¹² It, therefore, appears that the negative reaction to the announcement of the rehiring decision is not an assessment of the quality of the comeback CEO. He appears to perform as well as a CEO of a different firm from the same industry with a similar accounting performance in year $t - 1$.

Overall, one plausible interpretation of our announcement return evidence is that market participants learn from the announcement that the current, internally groomed CEO must have made such poor strategic decisions that he was untenable and needed to be replaced quickly (the average tenure is less than two years). Moreover, no external candidate was available or willing to take the job. Rehiring the former CEO may further signal to the market that there is no internal candidate, and this leads to a re-assessment of the firm's viability.

4.2.3. Do firms with former CEOs make different investment decisions?

In most cases (71%) in which a firm retains the former CEO, the current CEO was an employee of the firm, who was likely groomed by the former CEO and the board of directors for his new position (e.g., Naveen (2006) and Vancil (1987)). Our results indicate that stock performance rapidly deteriorates under his tenure (see table 2). Is it then a case of a fundamental misjudgment of the talent of the internal candidate, or could the former CEO be partially responsible for the current CEO's problems? Several business press articles argue that former CEOs may have undermined the current CEO's authority by their continuing involvement in their prior firms. For example, Olian (2003) suggests that there is a fine line between sitting on the board to provide advice when asked, versus diminishing the current CEO's authority by forcing his own opinion on the management team.

¹² The results are quantitatively and qualitatively similar if we use means instead.

Table 7 attempts to shed light at this issue by reporting the correlation coefficients for corporate policies across CEO turnovers. For each corporate policy and each firm, we calculate the average of the corporate policy for the last two years the former CEO was in office and the first two years that the current CEO (his successor) is in office. The first column reports the correlation coefficients for different policies for the sample of firms in which the former CEO does not stay on the board. The second column reports the correlation coefficients for the sample in which the former CEO stays on the board. The third column reports the z-value of a statistical test of the equality of correlation coefficients across the two groups of firms, based on Fisher's Z transformation (Fisher (1970)). A negative z-value implies that the correlation coefficient of the corporate policy across the turnover is higher for the sample with former CEOs on the board.

Overall, the results in table 7 suggest that corporate policies in firms in which the former CEO sits on the board are more correlated across a CEO turnover. In all but one case in which the z-value is statistically significant, the correlation coefficient of the corporate policy across turnover is higher for the group of firms in which the former CEO stays on the board. For example, while low, the correlation coefficient for acquisitions is 0.12 for the group of firms in which the former CEO does not stay on the board and 0.365 where the former CEO stays on the board. Weisbach (1995) found that turnover allowed for a change in acquisition policies through the divestiture of assets. The higher correlation in acquisitions suggests that these divestitures of assets would be less likely to occur in the group in which the former CEO sits on the board.

In general, the results in table 7 are consistent with the notion that it is more difficult to implement changes in corporate policies when the former CEO sits on the board of directors.

4.2.4. *Former CEO on the board and external hires*

If the current CEO partially failed because a strong, successful former CEO continued to sit on the board of directors, weakening the position of the current CEO and interfering with his strategic plan, and if it is particularly easy to influence an internal candidate who had worked under the strong prior CEO, the sub-sample of rehired CEOs provides a unique opportunity to study whether the board learned from previous decisions. It is informative to study what happens at the time the rehired former CEO steps down for the second time. Specifically, does the rehired former CEO retire for good and give up all positions within the firm? Or, is an outside CEO appointed? We have 38 cases of rehired CEOs for which we can retrieve information on the second retirement and the succession event.

The majority (66%) of the CEOs following the rehired CEO's second tenure are external appointments, which compares to only 29% external appointments at their first retirement. The percentage of rehired former CEOs who remain on the board of directors or who remain chairman of the BOD is still large with 68.4% and 57.9%, respectively, but smaller than at the first retirement, where 83% remained as chairmen and, by sample construction, all were board members.¹³ Interestingly, the correlation coefficient between hiring an outside CEO and the rehired former CEO continuing in office is -0.25. One explanation that is consistent with the negative correlation is that an external CEO tends to only accept the appointment if the powerful former CEO resigns from the board of directors so that a clean transfer of responsibility and power is assured.

¹³ We may overstate the continuing board membership of the retired CEO if he merely finishes his term on a staggered board, and then resigns.

5. Conclusion

Forty three percent of retired CEOs remain on the board of directors two years after their retirement, while 32% are on the board at the time of the turnover of their successor. In this paper, we revisit the determinants of a former CEO remaining on the board after retirement and study the consequences of this decision. Similar to Brickley, Linck, and Coles (1999), we find that the tenure of the CEO, stock market performance and founder status of the CEO are strong predictors of the probability that a former CEO remains on the board after retirement.

We study whether the presence of a former CEO on the board impacts two managerial hiring decisions. First, using a Cox proportional hazard model, we examine the impact of the presence of the former CEO on the board on the successor CEO's tenure. Controlling for stock market performance and other characteristics of the successor CEO and the firm, we find that tenure of the successor CEO is shorter if the former CEO is on the board at the time of the successor CEO's turnover. This is consistent with the former CEO being able to recognize a poorly performing CEO and move for his dismissal.

Second, approximately 10.5% of our sample firms rehire their former CEO. Having controlled for the probability that a former CEO sits on the board, we examine the determinants of decision to rehire the former CEO. Firms with former CEOs on the board have an option to rehire an available candidate. This option will be more valuable the lower is the firm's performance under the current CEO. Additionally, if the labor market for CEOs is characterized by scarce supply, then poorly performing firms with former CEOs on the board may be quicker to exercise this option. Having controlled for the probability that former CEO sits on the board, we show that a firm is more likely to rehire the former CEO if the firm is performing particularly poorly and if the former CEO was still involved in the firm, either because he was retired for a

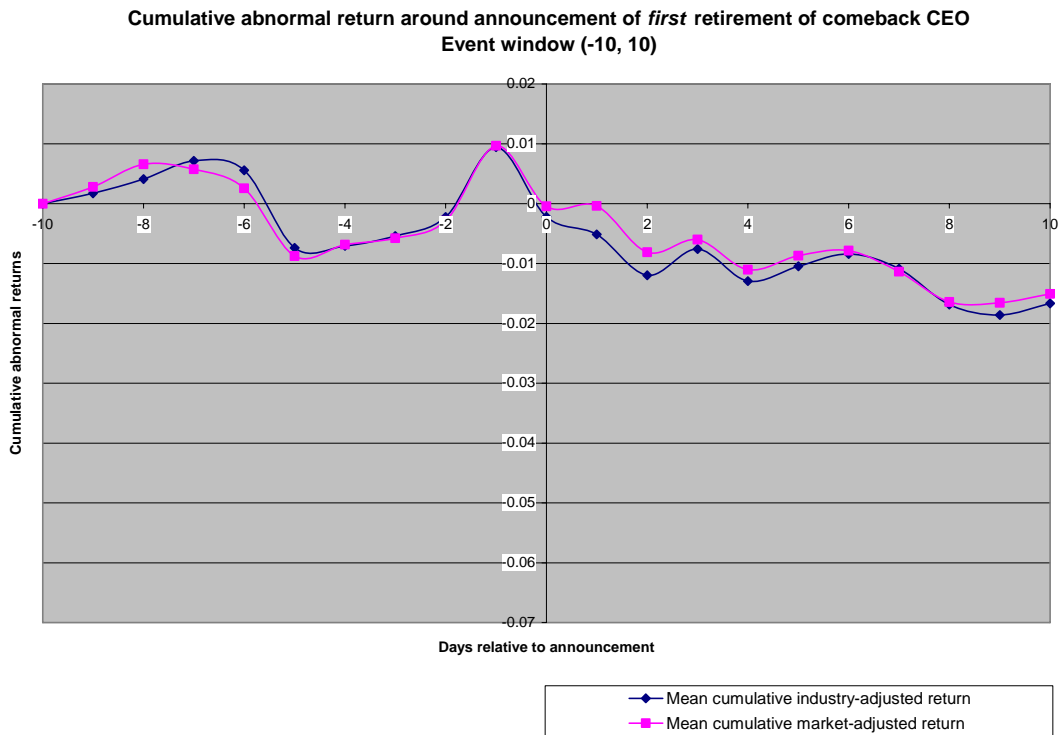
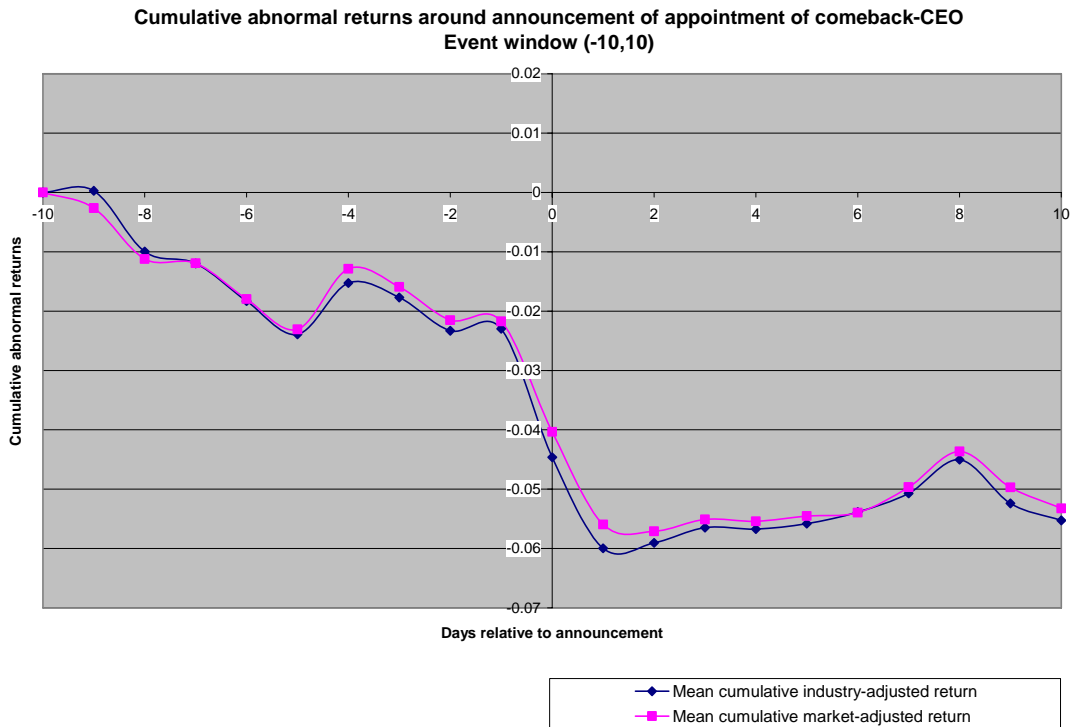
short period or chairman of the board. The market reacts negatively to the rehiring announcement. However, additional tests show that the negative cumulative return is not driven by the market's assessment about the quality of the comeback CEO. Overall, the return evidence is consistent with the notion that the internally groomed CEO made poor strategic decisions and needed to be replaced rapidly. The rehiring of the former CEO signals that no other candidate, either internal or external, was available or willing to take the job, and this leads to a re-assessment of the firm's future viability.

Retaining a former CEO, however, appears not without cost. Weisbach (1995) concludes that CEO turnover is important because it is part of the process of reversing managerial motivated acquisitions. We examine corporate policies in firms with and without the former CEO as a director. If the former CEO on the board has a strong presence, we might expect not to see changes in corporate policies. Overall, we find that corporate policies in firms with former CEOs on the board are more correlated across CEOs than in firms without former CEOs on the board. This result is consistent with the notion that it is more difficult to implement changes in corporate policies when the former CEO sits on the board.

Finally, another potential cost of having a former CEO on the board is the reluctance of an external hire to join the firm. We exploit the fact that we can observe two turnovers of the same CEO when a former CEO was rehired to examine this cost. In most cases of rehiring the former CEO, the current CEO was an internal candidate of the firm. If the current CEO partially failed because a strong successful former CEO continued on the board, weakening the position of the current CEO, it is informative to study whether the board makes different decisions when the rehired CEO retires the second time. There are 38 cases in which this occurs. In the majority of these cases, the firm hires an external candidate and the correlation between hiring an external

CEO and the rehired CEO remaining on the board is negative and significant. This negative correlation is consistent with the idea that an external CEO tends only to accept the CEO position if the powerful former CEO resigns from the board so that a clean transfer of power is assured.

Figure 1: Stock market performance event returns



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Table 1: Frequency of CEO Turnovers and Former CEO-directors

The Table lists the number of CEO turnovers of our sample, by year. The sample construction is described in detail in section 2. The first column of the table shows the total number of turnovers in our sample. The second (third) column lists the number of turnovers after which the former CEO stayed on the board of directors for at least one year (two years). The fourth column lists the number of turnovers in which the former CEO is still a member of the board of directors at the time his successor is turned over. The last column reports the number of cases in which the former CEO is still a member of the board of directors at the time his successor is turned over, and in which the former CEO is rehired as CEO.

Year	Total	Former CEO is Director			
		after 1 year	after 2 years	at turnover of successor	at turnover and rehired
1995	46	27	23	20	7
1996	56	32	22	17	7
1997	49	31	23	19	6
1998	60	33	25	20	6
1999	86	53	39	30	9
2000	83	45	33	25	9
2001	71	43	34	22	7
2002	87	49	42	26	8
2003	90	46	29	19	6
2004	13	8	6	7	2
Total	641	367	276	205	67
% of total	100.0%	57.3%	43.1%	32.0%	10.5%

Table 2: CEO Characteristics

The Table shows means and medians of CEO characteristics for sample firms. The first two columns show means and medians for the sample in which the former CEO was a director at the turnover of his successor. The third and fourth column shows statistics for all other turnovers of our sample. The last two columns contain p-values of tests of statistical differences in means and medians across the two groups. Tenure is the duration in years of the appointment as CEO. Share ownership is the fractional ownership of the CEO taken from the last proxy statement of his tenure. Founder of the company is a dummy variable equal to one if the prior CEO founded the firm and zero otherwise. Market-adjusted excess return is the annualized return in excess of the value-weighted market return of the CEO, annualized over his entire tenure. Age at turnover date is the age of the former CEO on the day of the successor CEO's appointment. Chairman of the board is an indicator variable equal to one if the last proxy statement prior to the appointment date of the successor CEO states that the former CEO was chairman of the board, and zero otherwise. Internal hire is an indicator variable equal to one if the current CEO worked for the company for at least 365 days prior to the appointment as CEO. All data are from ExecuComp, CRSP, and proxy statements.

	Former CEO director		Former CEO not dir.		Test of difference	
	Mean	Median	Mean	Median	Mean	Median
Former CEO						
Tenure	10.57	7.92	7.62	5.75	<.0001	<.0001
Founder status	0.30	0.00	0.10	0.00	<.0001	<.0001
Share ownership	0.05	0.01	0.02	0.00	<.0001	<.0001
Retirement age	59.63	60.92	56.77	56.63	<.0001	<.0001
Chairman of board at turnover of successor	0.65		---	---	<.0001	<.0001
Excess return	0.02	0.02	-0.08	-0.04	<.0001	<.0001
Current CEO						
Age at appointment	51.95	52.00	54.29	54.00	0.0004	0.0004
Tenure	2.62	1.95	3.41	3.00	<.0001	<.0001
Internal hire	0.71	1.00	0.66	1.00	0.1836	0.1904
Excess return	-0.19	-0.17	-0.14	-0.12	0.1176	0.0832
Excess return last year	-0.22	-0.24	-0.11	-0.15	0.0113	0.0133
Successor CEO						
Tenure	4.13	3.37	3.62	3.00	0.0262	0.1074

Table 3: Firm Characteristics of Sample Firms

The Table contains summary statistics for accounting variables and measures of firm complexity. The first two columns show means and medians for the sample in which the former CEO was a director at the turnover of his successor. The third and fourth column shows statistics for all other turnovers of our sample. The last two columns contain p-values of tests of statistical differences in means and medians across the two groups. The accounting variables are measured immediately prior to the resignation of the short-tenure CEO. All variables are defined in Appendix A.

	Former CEO director		Former CEO not dir.		Test of difference	
	Mean	Median	Mean	Median	Mean	Median
Total assets	5173.34	1045.27	8233.97	1521.88	0.005	0.034
Market-to-book	2.77	1.91	2.44	1.64	0.162	0.011
Sales growth	0.14	0.07	0.06	0.02	0.006	0.002
Capex / assets	0.06	0.04	0.05	0.04	0.587	0.592
Net PPE / assets	0.29	0.23	0.30	0.24	0.610	0.446
R&D / sales	0.11	0.04	0.10	0.04	0.842	0.622
Market leverage	0.25	0.18	0.31	0.24	0.007	0.023
Dividend Payer	0.49	0.00	0.54	1.00	0.239	0.239
Dividend	0.29	0.00	0.39	0.12	0.021	0.073
Return on assets	0.11	0.12	0.10	0.11	0.077	0.053
Industry homogeneity	0.17	0.14	0.18	0.14	0.582	0.553
High tech indicator	0.12	0.00	0.16	0.00	0.148	0.166

Table 4: Determinants of Continuing Board Service of the Former CEO

The Table reports results from Probit regressions of the likelihood that a former CEO is appointed to the board of directors of his former firm after retirement. The dependent variable is equal to one if the former CEO sits on the board for at least one year after retirement (column 1), at least two years after retirement (column 2), or until the turnover of his successor (column 3). The sample is described in section 2. The Table reports *marginal* effects. All variables are defined in Appendix A. Standard errors are corrected for heteroscedasticity and are reported in parentheses. The regressions also contain year-fixed effects and an indicator variable capturing missing information for CEO share ownership (not reported). Statistical significance at the 1%, 5%, and 10% level is indicated by ***, **, and *, respectively.

	Former CEO is board member		
	1 year after retirement	2 years after retirement	at turnover of successor
Return on assets	-0.047 (0.109)	-0.099 (0.108)	-0.077 (0.110)
Abnormal stock return	0.295*** (0.088)	0.273*** (0.089)	0.224*** (0.079)
CEO tenure	0.009** (0.004)	0.008** (0.003)	0.006** (0.003)
Founder indicator variable	0.130** (0.062)	0.136** (0.067)	0.181*** (0.067)
Percentage of stock held	0.077 (0.423)	0.651 (0.396)	0.624* (0.348)
Log (assets)	0.002 (0.013)	-0.014 (0.013)	-0.014 (0.012)
Age of successor CEO	-0.011*** (0.003)	-0.007** (0.003)	-0.005** (0.002)
Successor CEO internal appointment	0.118** (0.046)	0.139*** (0.045)	0.051 (0.042)
Number of observations	597	597	597
Observed probability	0.586	0.442	0.320
Estimated probability	0.594	0.427	0.303
Pseudo R-squared	0.094	0.096	0.097

Table 5: Effect of CEO and Firm Characteristics on the Tenure of the CEO

The Table reports results from a Cox proportional hazard model of the tenure of the current CEO. Each CEO's career is treated as a single observation. Since our sample construction requires a turnover of the current CEO, the Cox proportional hazard model is estimated with uncensored data; every observation has a failure event (i.e., the CEOs employment contract is terminated). The dependent variable is the total number of months the current CEO serves as CEO. The table reports hazard ratios. A coefficient larger than 1 indicates that an increase in the independent variable leads to an increase in the probability of failure (i.e., to a decrease in CEO tenure). The first column includes all observations and independent variables that are measured at the time of the appointment of the current CEO. The second column reports controls for characteristics of the former CEO and includes hazard ratios for two other additional variables: Whether the former CEO stayed on the board of directors and an indicator variable equal to one if the current CEO's performance was in the lowest quartile. The third column adds an indicator variable equal to one if the former CEO sits on the board at the time his successor is turned over. All other independent variables are defined in Appendix A. Standard errors are reported in parentheses. Statistical significance at the 1%, 5%, and 10% level is indicated by ***, **, and *, respectively.

	base-case	Former CEO is director			
		1 year after retirement		at turnover of successor	
Current CEO internal appointment	0.838** (0.073)	0.869 (0.079)	0.853* (0.077)	0.829** (0.073)	0.819** (0.072)
Current CEO age at appointment	1.013** (0.006)	1.016** (0.006)	1.015** (0.006)	1.020*** (0.006)	1.019*** (0.006)
Log (assets)	0.942** (0.022)	0.941*** (0.022)	0.946** (0.022)	0.958* (0.023)	0.964 (0.024)
High-tech indicator variable	1.138 (0.129)	1.145 (0.131)	1.155 (0.133)	1.205 (0.138)	1.220* (0.140)
Industry homogeneity	0.302** (0.145)	0.288** (0.140)	0.319** (0.155)	0.241*** (0.118)	0.263*** (0.129)
Current CEO's return in last year of tenure		0.683*** (0.068)		0.710*** (0.070)	
Current CEO's return in bottom quartile			1.330*** (0.129)		1.311*** (0.126)
Former CEO sits on board for at least 1 yr		0.856* (0.072)	0.874 (0.074)		
Former CEO sits on board at turnover of current CEO				1.408*** (0.128)	1.429*** (0.130)
Observations	622	608	608	608	608

Table 6: Determinants of the Decision to Rehire the Former CEO

The Table reports results from a two-stage Heckman selection model. The first stage estimates the determinants of the decision of the former CEO to stay on the board of directors until the turnover of his successor. It is estimated for the entire sample. The results, for completeness, are reported in the column 'selection equation'. The second stage models the probability that the former CEO returns to the position of CEO, given that we observe a data point in which the former CEO is a board member at the turnover of his successor. All independent variables are described in Appendix A. Standard errors are reported in parentheses. Statistical significance at the 1%, 5%, and 10% level is indicated by ***, **, and *, respectively. The Wald test of independence is a chi-square test of independence of the principal and selection equations.

Selection Equation		Principal Equation	
Former CEO ROA	-0.086 (0.283)	Former CEO retirement age	0.003 (0.004)
Former CEO abnormal stock performance	0.643*** (0.223)	Former CEO years in retirement	-0.041*** (0.014)
Former CEO tenure	0.017** (0.008)	Former CEO top quartile performer	-0.057 (0.077)
Former CEO founder	0.470*** (0.169)	Former CEO founder	-0.043 (0.090)
Former CEO stock ownership	1.600* (0.969)	Former CEO stock ownership	-0.044 (0.458)
Log (assets)	-0.070** (0.033)	Former CEO chairman of the board	0.209*** (0.070)
Successor CEO internal appointment		Current CEO was internal appointment	0.135* (0.080)
Successor CEO age at appointment	-0.019*** (0.007)	Current CEO bottom quartile performer	0.175** (0.070)
		Net PPE / assets	-0.135 (0.171)
		Capex / assets	0.082 (0.860)
		R&D / sales	-0.112 (0.121)
		No R&D reported dummy	-0.162** (0.068)
		Log (assets)	0.057*** (0.020)
		High tech indicator	-0.060 (0.077)
Wald test of independence of selection equation and principal equation (p-value)	0.006***		

Table 7: Correlations in Corporate Policies Across CEO turnovers

The table shows the correlation coefficients for corporate policies across turnovers. For each corporate policy and each firm, we calculate the average of the corporate policy for the two last years the former CEO was in office and the two first years the current CEO was in office. If the current CEO has a tenure of less than two years, we only include data while he was in office. The first column reports correlation coefficients for different policies for the subsample of firms in which the former CEO did not stay on the board for at least two years after retirement, and the second column reports correlation coefficients for the subsample of firms in which the former CEO stayed on the board of directors. The third column contains the z-value of a statistical test of equality of correlation coefficients across the two subsamples, based on Fisher's Z transformation (Fisher (1970)). A negative and statistically significant z-value implies that the correlation of the corporate policy across the turnover is higher for the subsample with former CEOs on the board of directors. Statistical significance at the 1%, 5%, and 10% level is indicated by ***, **, and *, respectively.

Corporate policy	Correlation coefficients pre- turnover/post-turnover		Test of equality of corr. coeff. across columns 1 and 2	
	No former CEO on board	Former CEO on board	Fisher's z	p-value
Dividends	0.909	0.945	-3.230	0.001***
Capex / assets	0.599	0.754	-3.478	0.001***
Acquisition / assets	0.120	0.365	-3.028	0.002***
R&D / sales	0.880	0.939	-3.317	0.001***
Sales growth	0.174	0.320	-1.876	0.061*
Asset growth	0.072	0.230	-1.966	0.049**
Book leverage	0.796	0.802	-0.201	0.841
Market leverage	0.869	0.830	1.758	0.079*
PPE / assets	0.957	0.974	-3.298	0.001***
Profit margin	0.890	0.917	-1.810	0.070*
SG&A / sales	0.947	0.921	2.243	0.025**
Cash / assets	0.844	0.856	-0.540	0.589
Advertising / sales	0.856	0.931	-2.001	0.045**
Number of employees	0.9475	0.969	-3.266	0.001***

Appendix A: Variable definitions

This appendix describes the COMPUSTAT variables we used in our analysis. When calculating the ratios, the variables are taken from the same COMPUSTAT year unless specified otherwise.

Derived Variables:

BE (Book value of Equity) = Shareholders' equity (216) [or Common equity (60) + Preferred stock carrying value (130) or Assets (6) - Total liabilities (181)] – Preferred stock liquidating value (10) [or Preferred stock redemption value (56), or Preferred stock carrying value (130)];

ME (Market value of Equity) = Fiscal year end market price (199) * Common shares outstanding (25);

Y (Income available to common shareholders) = Income before extraordinary items (18) – Preferred dividends (19) + Deferred taxes (50) if available;

V (Total firm value) = Total assets (6) – BE + ME;

Debt = Long-term debt (9) + Debt in current liabilities (34);

EBIT (Earnings before interest and taxes) = Income before extraordinary items (18) + Interest expenses (15) + Income taxes (16)

Ratios:

Acquisitions / Assets = Acquisition costs (129) / Assets (6);

Asset Growth_t = Assets (6)_t / Assets (6)_{t-1} - 1;

Book Leverage ratio = Debt / (Debt + BE);

CAPEX / Assets = Capital expenditure (128) / Assets (6);

Cash / Assets = Cash (36) / Assets (6);

Interest coverage ratio = EBIT / INT (15);

Market-to-book ratio = ME / BE;

Net PPE / Assets = Net PP&E (8) / Assets (6);

Operating Cash flow = EBITDA (13), plus decrease in accounts receivable (item 2), plus decrease in inventory (item 3), plus increase in accounts payable (item 70), plus increase in other current liabilities (item 72), plus decrease in other current assets (item 68) / Assets (6)

Profit margin = EBITDA (13) / Sales (12);

R&D / Sales = R&D expenditure (46) / Sales (12);

ROA = EBITDA (13) / Assets (6)

ROE = Y / BE;

Sales Growth_t = Sales (12)_t / Sales (12)_{t-1} - 1;

SG&A / sales = SG&A (189) / Sales (12);