EXECUTIVE LAWYERS: GATEKEEPERS OR TOTEMS OF GOVERNANCE?

ADAIR MORSE*

WEI WANG

SERENA WU

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Abstract

Lawyers now serve as executives in 44% of corporations. Although endowed with gatekeeping titles and responsibilities, these lawyers face increasing tension on their time to add strategic legal input into business development. We quantify lawyer importance along these dimensions. Lawyer fixed effects explain 3.5% of the across-firm variation in regulatory compliance, 10% in monitoring failures, and 3.3% in business development over and above firm and year fixed effects. These effects are 20-60% as large as CEO effects in our sample, and thus quite material. Our main contribution compares executive lawyers hired from law firms (who face more reputational capital exposure) to lawyers poached from corporations to ask whether firms' optimal contracting of lawyers to induce strategic input implies lower lawyer attention to gatekeeping. We find that lawyers with a standard deviation higher compensation delta (indicative of the importance of strategic goals in compensation contracts) prevent 67% fewer class action frauds and 48% fewer general lawsuits compared to the average gain associated with hiring an executive gatekeeper. Reassuringly, lawyers do not compromise regulatory compliance.

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"*Lawyers are what today we call crucial gatekeepers, responsible for safeguarding shareholders' interests*"
– Former SEC Chairman Christopher Cox[1]

"I have been there at the beginning of an idea, I have helped implement the idea, and on those occasions where an idea has turned out poorly, I was there to help clean up the mess, too."
– Peter Bragdon, SVP, General Counsel, and Secretary of Columbia Sportswear Company[2]

I. Introduction

The office of general counsel (or chief legal officer) is arguably the most important internal governance actor in the firm. The top internal lawyer in corporations now sits among the top five executives in over 44% of U.S. public corporations. Conditional on being in the inner suite, executive lawyers earn 43% of CEO compensation. What makes these executive lawyers unique in firm leadership is their dual role as strategic officers and gatekeeping agents. As our title suggests, our main goal is to explore whether the call to add strategic input into business development affects executive lawyers' gatekeeping such that they become simply totems of governance. We use the terminology "totems of governance" to respectfully depict that, in their title, executive lawyers command the strongest possible emblem of internal governance, even if, for some companies, the emblem of governance is a majestic relic of times past.

Executive lawyers' tasks fall into three dimensions – regulatory compliance, governance monitoring and business development (Demott, 2005; Heineman, 2012; Sorkin, 2012).[3] An important accounting literature documents the regulatory compliance role of lawyers. Jagolinzer, Larcker, and Taylor (2011), Krishnan, Wen, and Zhao (2011), Kwak, et al. (2012), Hopkins, Maydew, and Venkatachalam (2015), and Goh, Lee and Ng (2015) collectively study the effect of the quality of lawyer

1 Address to the Corporate Counsel Institute, March, 8, 2007
[2] See Dubey and Kripalani (2013) – page 42.
[3] Regulatory compliance refers to compliance breaches that risk investigation and/or allegation of regulatory bodies, such as SEC or IRS. Other breaches are categorized into governance monitoring. Note that the classification is not based on whether the breaches are detected, but rather whether it involves regulatory scrutiny. We later refer to regulatory compliance and governance monitoring together as gatekeeping. Some internal governance breaches may lead to regulatory enforcement ex post. For example, the option backdating scandals in 2005-2006 triggered SEC allegations and many executives, including general counsels, experienced forced turnover as a result (Efendi, Files, Ouyang, and Swanson, 2013).

reputation on the likelihood of compliance breaches to accounting standards and regulations. Choudhary, Schloetzer, and Sturgess (2013) extend this analysis to outside legal counsels. This compliance function is surely important for executive lawyers. In the surveys of Deloitte (2011) and KPMG (2012), roughly two-thirds of general counsels cite maintaining regulatory compliance as their greatest concern. But compliance is just one of three roles of the general counsel.

In their second role, that of internal governance monitors, general counsels watch for firm or executive infractions not covered in regulatory compliance. The trend of greater lawyer prominence inside the firm comes during a period when firms have become more interested in policing themselves, following hostile takeovers of the 1980s, the Sarbanes-Oxley Act (SOX) in the early 2000s, the Dodd-Frank legislation subsequent to the financial crisis starting in 2008, and most recently, shareholder activism. Executives and the board consult executive lawyers on matters such as antitrust, the disclosure of material information, affiliated transactions, consumer liability, etc. Evidence for the role of executive lawyers in litigation comes from Kwak, et al. (2012), who include the appointment of a new general counsel as a factor in predicting litigation risk.

In their third role, that of strategic officers, executive lawyers offer their legal expertise as an input into business development and risk management (Sorkin, 2012). An example we like to give is that one can imagine being a CEO or director of a company such as Apple. Surely one would want legal expertise on the business development team to think about future patent claims and infringements before choosing the next innovation strategy. Russell Reynolds Associates (2013) analyzed their database of 3,000 assessments of corporate executive and found that "*contrary to conventional wisdom, the legal executives go well beyond spotting legal issues to helping the business actually take risks and find creative solutions.*"

Our first empirical analyses gauge the importance of executive lawyers in these multiple tasks, providing empirical support for the legal literature on lawyers as gatekeepers (e.g., Nelson and Nielsen, 2000; Coffee, 2003; DeMott, 2005; Heineman, 2012; Sorkin, 2012). We measure regulatory compliance failures with Accounting and Auditing Enforcement Releases (AAERs) and allegations of insider trading

made by the Securities and Exchange Commission (SEC); monitoring failures with securities fraud and general lawsuits; and business development with capital expenditure intensity, R&D, and business complexity. In an individual fixed effects analysis following Bertrand and Schoar (2003), we find that lawyer fixed effects absorb 3.5% additional variance (partial r-square) in regulatory compliance, 10% in monitoring failures, and 3.3% in business development, over and above firm and year fixed effects. Our results are robust to the control of CEO fixed effects. These magnitudes are 20-60% of the size of CEO fixed effects that are above the firm and year fixed effects, and thus quite material.

Interpreting the lawyer fixed effects results with generalizable causality language may be problematic as the estimates come from the selection of lawyers that move. Thus, for robustness, we run propensity-score-matched, difference-in-differences tests around the hiring of an executive lawyer into the firm. This design has an opposite selection bias concern, where the choice to hire is based on unobservables such as the future need for gatekeeping. In other words, one analysis errs on only estimating with the set of hires and thus may not be general, and the other analysis may err on not being able to control for all unobservables in the decision to hire. Taken together, however, consistency in the estimates across methods suggests a causal relationship between the existence of an executive lawyer and stronger compliance and monitoring. We infer that executive lawyers are indeed gatekeepers.

Our main agenda is to ask whether executive lawyers trade off some of this gatekeeping when they have incentive contracts designed to reward business development effort rather than gatekeeping. We are not saying that effort toward business development is suboptimal from a firm's perspective, but rather that the title of general counsel may become a totem for society looking for full gatekeeping assurances. The theoretic intuition behind our multi-task story is the following setup. Imagine an executive lawyer is paid with salary and equity incentives, has limited time, and faces the possibility of a career-ending governance breach. A governance breach also has dire consequences to firm value, but otherwise, gatekeeping creates no firm value. Motivated by the accounting compliance literature, we assume that the probability of a governance breach grows convexly large as gatekeeping time decreases, but is relatively insensitive to gatekeeping time once the lawyer is already a somewhat diligent gatekeeper. By contrast,

when executive lawyers spend time in business development, the effort always generates firm value. Thus, equity incentives will tilt executive lawyers toward business development in most settings. Firms heterogeneously choose optimal amounts of equity incentives to achieve their optimal mixture of gatekeeping time and business development time. This intuition aligns with our understanding of firm processes. However, we need not assume this optimal contracting intuition. An alternative interpretation is that a lawyer may be distorted away from optimal gatekeeping with equity incentives that the firm is forced to offer in the labor market for lawyer officers. Either story fits with our empirical design, but we use the optimal contracting terminology.

Our identification exploits a comparison of two sets of corporations hiring executive lawyers. The first set poaches existing corporate lawyers from other companies (treated), and the second set hires executive lawyers from law firms (control). Our key assumption is that equity incentives are *initially* less likely to divert newly-hired law firm lawyers away from gatekeeping, compared to their corporate hired peers. The intuition is that law firm lawyers (i) exhibit loyalty to their professional association (Goode, 1957; Hall, 1968; Wallace, 1995), (ii) must go through a learning curve to understand the business development strategy of the firm, (iii) must change their habit as a lawyer and learn to be more comfortable with risk, a contrast to their training to practice risk-aversion (Dubey and Kripalani, 2013), and (iv) must be willing to step away from their stock of reputational capital.

We use this assumption in collapsed, double and triple differenced designs that allow us to assert a plausible casual identification of the effects of business development incentives (measured by equity incentives) on gatekeeping. Both the treated and the control are firms hiring executive lawyers; we therefore avoid the endogeneity of whether or not an executive lawyer is hired. The source of hiring, however, is endogenous. We use propensity score matching within year-industry buckets to level treated and control firms on observable predictors of past and future needs for regulatory compliance, monitoring and business development. To the extent that unobservables remain in the choice of hiring source, we simply control for them since our identification comes from the interaction of equity incentives with the

source of hiring. A residual identification concern is that the use of equity incentives is correlated with our outcomes in a way systematic of hiring source. We address such concern in robustness.

We find that higher corporate equity incentives imply materially lower governance monitoring. Our empirical design suggests that such evidence can be plausibly interpreted as causal in the relationship between the optimal contracting of executive lawyers that induces more effort in business development and the lowering of governance monitoring. Corporations providing executive lawyers with one standard deviation higher equity incentives have 1.3 percentage points higher likelihood of securities fraud (a 28% percentage change) and 1.2 percentage points higher likelihood of general lawsuits (a 14% percentage change). We interpret the magnitude relative to the benefit of having an executive lawyer gatekeeper: when firms strongly contract executive lawyers to be strategic officers, they unwind 67% of the governance improvements in terms of avoiding securities fraud and 48% of the governance improvements in avoiding general lawsuits that are associated with the hiring of an executive gatekeeper.

On the flip side of the tradeoff of executive lawyers' time, we find some, but weak, evidence that equity incentives induce executive lawyers to exert more effort on business development. We interpret the evidence with caution. The effort of business development can be manifested in many different dimensions thus hard to be captured with specific outcome measures. We find no support for equity incentives affecting regulatory compliance, consistent with the literature we cite herein on the dire consequences of compliance infractions for corporate lawyers.

Our study contributes to the new internal governance literature of Acharya, Myers, and Rajan, (2011), Kim and Lu (2012), and Khanna, Kim and Lu (2015). Arguably, the largest internal governance actor or gatekeeper is the general counsel; this important facet of internal governance warrants a big-picture study that looks at its overall effectiveness as well as its interaction with equity incentives. A recent legal literature (Duggin, 2006; Rostain, 2008; Demott, 2012) outlines the compliance and monitoring roles of general counsel. We build on the legal description of lawyer's jobs in corporations and test whether the actions of general counsels are effective. We contribute to a small but growing body of empirical studies on in-house lawyers (Jagolinzer, et al, 2011; Kwak, et al., 2012; Hopkins, et al, 2015;

Goh, et al., 2015), which focus on the regulatory compliance role of the lawyers, by adding evidence on the governance role and strategic development role with a focus on the trade-off between the two.[4]

Our study also adds executive lawyers to the literature on the importance of characteristics of individuals inside the executive suite (e.g., Bertrand and Schoar, 2003; Malmendier and Tate, 2009; Custodio and Metzer, 2014). We show that individual lawyers matter. Concurrently, Krishnan and Masulis (2013) and Karsten, Malmendier and Sautner (2014) take up this question for external lawyers, asking whether lawyer quality affects acquisition outcomes.

The rest of the paper is organized as follows. Section two provides background on the roles of executive lawyers. Section three describes data construction and sources. Section four quantifies the importance of executive lawyers across their compliance, monitoring, and business development tasks. Section five tests for whether the call to be a strategic officer compromises gatekeeping, i.e., the gatekeeper versus totem tests. Section six concludes.

II. The Roles of Executive Lawyers

II.a. Compliance officer

Maintaining compliance in financial and regulatory filings on a daily basis is the compulsory role of executive lawyers (Lipson, Engel, and Crespo, 2012). Compliance breaches are the greatest legal risk in the view of most executive lawyers; the top cited regulatory risks include SEC fraud investigations, insider trading, and stock market disclosure (Deloitte, 2011; KPMG, 2012). This is not surprising given the steep reputation costs to infractions of compliance. Desai, Hogan, and Wilkins (2006) find that 60 percent of earnings restating firms experience a turnover of at least one top manager within 24 months of the restatement compared to 35 percent among matched firms. Karpoff, Lee, and Martin (2008) track individuals that the SEC and DOJ identify as responsible parties for enforcement actions concerning financial misrepresentation. They find that 93% of these individuals lose their jobs by the end of the

[4] Our study is also related to Litov, Sepe, and Whitehead (2014), who study the governance effect of lawyers in the board of directors.

regulatory enforcement period. Most are explicitly fired. Moreover, if managers are alleged to be responsible directly for the misconduct, they not only lose their jobs and bear substantial financial losses but also can face criminal charges and even jail sentences. On the flip side, recent papers in the accounting literature (Jagolinzer, et al., 2011; Kwak, et al., 2012) find that lawyer prestige associates with more favorable compliance outcomes in insider trading and corporate earnings disclosure, suggesting, importantly, that compliance reputation is an upward career ladder for corporate lawyers.

II.b. Internal governance monitor

Beyond compliance, Demott (2005) describes general counsels' day-to-day duties as involving and bearing responsibility for *all* legal exposure affecting the corporation including such matters as customs and trade issues, and intellectual property infractions (Dubey and Kripalani, 2013). An executive lawyer views herself as "a guardian of the corporation's integrity and reputation" (Heineman 2007), perhaps because historically the SEC has laid governance breach liability on the position of the general counsel. The SOX Section 307 formalized these monitoring responsibilities by adopting rules whereby corporate lawyers are not just liable for compliance breaches, but are exposed as the office responsible for reporting evidence of material violation of securities laws or breaches of fiduciary duty "up-the-ladder" inside the firm.[5] In addition, SOX endowed the SEC with the necessary power to discipline corporate lawyers who are deemed to lack integrity or who have engaged in unethical or improper professional conduct. A case in point is former Apple general counsel Nancy Heinen, who not only paid $2.2 million to the SEC to settle backdating charges but was barred from appearing or practicing as an attorney before the commission for three years.

II.c. Strategic officer

[5] See http://www.sec.gov/rules/final/33-8185.htm.

"A General Counsel needs to be a business person first and a lawyer second—not a lawyer that understands the business, but a business person that happens to be a lawyer"

- Marla Persky, General Counsel of Boehringher Ingelheim Corporation[6]

A lessor understood role of an executive lawyer is as a strategic officer, adding planning and risk management input into expansion, innovation, and business development. The role of the executive lawyer has changed dramatically in a world with increasing importance of intangible assets and the information economy. Executive lawyers are often found to carry an official designation as a business or corporate development executive, on top of their legal designation of general counsel or chief legal officer. Bagley (2008) points out that firms characterize their executive lawyers more as entrepreneurs than policing lawyers. Executive lawyers are engaged in business development through the work done by the legal department's intellectual property teams (Dubey and Kripalani, 2013), from the earliest phases of business development (Demott, 2005) and throughout the planning and implementation process of investment (Horner, 2007). This view is echoed in practitioner surveys; executive lawyers that receive the best performance ratings are 11% more willing to take risks than the average executive lawyers, and they are as likely to take risks as any other executive (Russell Reynolds Associates, 2013).

III. Data

III.a. Executive lawyers and compensation

To identify the general counsel as a corporate officer, sometimes called chief legal officer, we look for individuals holding the requisite titles by manually reading executive titles from 10-K filings (items 4b and 10) or proxy statements for all firm years in ExecuComp, which covers firms in the S&P large, mid and small cap indices. Over our sample period 1995-2012, this includes 32,372 firm-year observations for more than 3,000 unique firms. We look for three key words: "Counsel," "Legal," and "Law" or abbreviations or variants. Then we read each signatory on the filings, as each company should

[6] See Dubey and Kripalani (2013).

have a lawyer that carries the responsibility of the legal signatory to the SEC. If such person is not listed as one of the executive officers, and the name signing the legal certification does not have a general counsel or chief legal officer designation, it is likely that the lawyer is not an important corporate officer in the firm. We further look to ExecuComp titles for the same legal recognition, just in case the legal counsel also holds another title which she uses to sign the SEC documents.[7] In our sample, 70 percent of firms on average have a general counsel as a corporate officer, relatively stable over time.[8]

In the main tests, we impose an additional attribute to designate general counsel in the inner executive office as executive lawyer (ExecLawyer). We apply a monetary proxy for the importance of the general counsel in the firm; individuals must be among the top paid officers in a company in ExecuComp. We force stringency that this proxy is not transitory in requiring that the officer remain in the top paid executives for three years.

Our main empirical design relies on the employment history of these ExecLawyers. We look up the full career path of work experience from law school graduation to prior to becoming ExecLawyer of a firm by hand collecting ExecLawyer's bios from corporate filings and online sources such as LinkedIn and law firm websites. We are able to identify the last work experience before becoming ExecLawyer for 2,446 of the total 2,630 ExecLawyers in our sample.

We use compensation data from ExecuComp for the ExecLawyer and CEO. We value option grants using the Black-Scholes model[9] and define total pay as the sum of salary, bonus, LTIP, other cash compensation, restricted stock grants and option grants. We follow Core and Guay (2002) to estimate the

[7] ExecuComp often records multiple titles. One issue with Execucomp is in its use of abbreviations of an executive title. For example, the title of a general counsel could be spelled as "gen cou," "gncns," "gen cns," etc. We add all versions of these words we can find. Further, the initial search of the three key words resulted in many executives who are not general counsels (e.g. "Special Counsel", "Former Counsel"). We verify whether the executive officer identified is in fact a general counsel of the firm through further reading their full executive titles.

[8] Our fixed effects analysis is based on this complete set of generate counsels as corporate officers, and thereby identifying lawyer fixed effects using all movers within our sample.

[9] We follow Core and Guay (2002) with minor modifications to estimate the grant date value of options. First, if the grant date is missing, it is assumed to be June 30 of that year. Option maturity is assumed to be seven years if the maturity date is missing. Second, the expected stock return volatility is measured as the annualized standard deviation of daily stock returns over the fiscal year in which the grant was made. Third, expected dividend yield is the ratio of cash dividends paid in the fiscal year of the grant and the fiscal year-end stock price. Finally, the Treasury bond yield corresponding to the option's expected time to maturity is used as the risk-free rate.

sensitivity of the value of the ExecLawyer's accumulated equity-based compensation (including both stocks and options) to a one-percent change in the stock price, which is referred to as "delta".[10]

III.b. Compliance failures

We measure the failures of regulatory compliance in two dimensions, both requiring the signature of the general counsel on forms – Accounting and Auditing Enforcement Releases (*AAERs*) and insider trading. AAERs are issued at the conclusion of an SEC investigation against a company, an auditor, or an officer for alleged accounting and/or auditing misconduct. We obtain AAERs data from the Center for Financial Reporting and Management Center at Berkeley Haas. We code the variable AAER to capture when the alleged accounting misconduct was taking place (known ex post) rather than when the enforcement action is launched. We exclude AAERs that are not related to misstatement (e.g., for reasons such as bribery and disclosure). Because it takes approximately a year and a half for frauds to emerge (Dyck, Morse, and Zingales, 2010) and another span of a year or two for the SEC to complete an investigation, we truncate analysis to 2009 when studying AAERs given that our sample ends in 2012.

Similarly, we measure insider trading using alleged cases. We manually collect alleged insider trading cases from SEC litigation releases and match them with our sample firms.[11] Thus the two compliance failure measures are both violation based, capturing the actual failure rather than the likelihood of compliance breaches as seen in prior studies on corporate lawyers (e.g. earnings management measures, insider trading profit measures, etc.).

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[10] In order to calculate delta, we require information on the number of shares and both the number and value of unexercised options held by the ExecLawyer. We find that ExecuComp often does not report the actual share ownership for non-CEO executives. In such cases, we assume the delta of stock holdings to be zero. Nevertheless, for robustness purpose, we perform additional multivariate tests by using the sub-sample after dropping delta that carries missing/zero values.

[11] The SEC litigation releases are publicly available on the SEC website: https://www.sec.gov/litigation/litreleases.shtml. These releases are summaries issued by the SEC that describe civil lawsuits brought by the Commission in federal court. We read litigation releases to uncover investigations involving insider trading as the reason for the suits. If a corporate executive is alleged to have traded his/her own company's stock based on insider information or have tipped such information for others to trade, then we code that firm year to be an insider trading year. A drawback is that the releases often do not record the exact dates when insider trading took place. We remove these cases.

III.c. Monitoring failures

We measure non-compliance internal governance breaches in three dimensions – securities fraud, general lawsuits, and option backdating. Securities class action lawsuits, a measure for securities fraud, involve more general misconduct than that caught in AAERs, with over 40% of securities fraud not related to misrepresentations in reporting but instead related to misleading or omissions in communication or self-dealing (Dyck, Morse and Zingales, 2010; 2014).[12] Data of these lawsuits come from the Stanford Law School Securities Class Action Clearinghouse. We use the overall set of securities fraud class actions cleansed of dismissed and unresolved cases.[13] There are altogether 1,187 lawsuits filed against public firms during this period, with 582 cases that were dismissed by the court and 78 that we remove for being unresolved.

The second lawsuit measure we use covers breaches of any law, including but not restricted to securities law. We collect general lawsuits data from Audit Analytics and purge suits that lead to AAERs and those with zero settlement. Examples of general lawsuits include suits arising from trademark or patent disputes, product liability, personal injury, labor disputes, commercial contracts, etc.

Our final monitoring measure is the backdating list published by the *Wall Street Journal*, identifying companies that have disclosed government probes on misdated options and related restatements as of September 2007.[14] We identify the year(s) when backdating breaches were occurring by reading the investigation reports.

III.d. Business development measures and other company outcomes

[12] See Karpoff, Koester, Lee, and Martin (2013) for a comparison of fraud data.

[13] To construct a securities fraud variable, we collect the class action lawsuits filed during 1995-2012 from the Stanford Law School Securities Class Action Clearing House and merge them to Compustat. The Stanford Law School Securities Class Action Clearing house database has been employed by a number of prior studies (e.g., Lowry and Shu, 2002; Field, Lowry, and Shu, 2005; Dyck, Morse, and Zingales, 2010; and Hanley and Hoberg, 2012). These securities frauds are alleged rather than proven, in that few cases ever get resolved in trail, but rather settle out of court, because D&O insurance does not cover the executives with court convictions.

[14] See http://online.wsj.com/public/resources/documents/info-optionsscore06-full.html

In choosing measures of business development, we focus on organic growth because corporations almost always hire external transaction lawyers for one-time events such as M&A or spinoffs (Krishnan and Masulis, 2013). The first measure is the ratio of capital expenditure to fixed assets at the beginning of the fiscal year, capturing investment intensity in tangible assets (Eisdorfer, 2008). The second measure is R&D expenses scaled by assets as a measure of investment intensity in intangible assets. The third measure is the number of business segments, capturing expansion in the line of business.

Our analysis also considers two typical measures of corporate governance, not related to lawyer activity, to consider the mechanism of our results. To strengthen the board, the shareholders may bring in more independent board members. We gather these data from Riskmetrics. We also obtain the G-index of Gompers, Ishii and Metrick (2003) from Riskmetrics to measure shareholder rights. A higher value of G-index indicates weaker shareholder monitoring.

Appendix Table 1 summarizes all of the variables listed in this section.

IV. The Importance of Lawyers

IV.a. Importance of lawyers: Statistics

Table 1 profiles General Counsel and ExecLawyers based on the ExecuComp sample of 32,372 firm-year observations and tabulated by fiscal years. The second and third columns respectively report the percentage of firms having a General Counsel as a corporate officer and having an ExecLawyer, identified in the annual filings data and in ExecuComp. In both series, we document a secular trend upwards. In the year 1995, 66% of the S&P 1,500 index firms had General Counsel as a corporate officer while 33% of the firm had an ExecLawyer; the percentage increases to 81% and 44%, respectively by the year 2012. Our numbers on ExecLawyer are a few percent lower than those reported in Kwak, et al. (2012), who document this pattern with the addition of legal affairs officers and some other variations such as legal or political officers. Conditional on having an ExecLawyer, the remaining statistics in Table 1 report that ExecLawyer compensation has increased as a fraction of CEO pay from 34% to 43%. Executive lawyers earn $1.445 million in constant 2012 dollars on average over the last two decades. For

every 1% increase in shareholder value, ExecLawyers make another $55,000 in equity income on average, a much smaller fraction (6%) of wealth performance sensitivity compared to the CEOs' delta. About one third of the ExecLawyer deltas are zero, a point we re-visit empirically.

IV.a. Importance of lawyers: Methodology

To measure to what extent differences among individual general counsels matter, we use a lawyer fixed effect model, following Bertrand and Schoar (2003), Malmendier and Tate (2009) and Custodio and Metgzer (2014). Bertrand and Schoar use the movement of executives across firms to gauge how much variation in the performance metrics of relevant firms is due to individual managers. A recent accounting literature applies this methodology to document significant top mangers' individual effects on firms' voluntary disclosures, tax avoidance, and a wide range of financial reporting choices (Bamber, Jiang and Wang, 2010; Jiang, Petroni, and Wang, 2010; Dyreng, Hanlon and Maydew, 2010; Ge, Matsumoto and Zhang, 2011).

We use this methodology to accomplish two goals. First, we build on the literatures studying general counsels by offering a quantification of the importance of individual lawyers across firms relative to the importance of CEOs. Second, we study the lawyer fixed effects in the multi-task dimensions of compliance, monitoring and business development to motivate our main agenda analysis of the multi-task tension and tradeoff that executive lawyers face.

In our implementation, we use all general counsels, not simply those we classify as being in the top executive offices by salary, because, not being constrained to have compensation data, we can more cleanly identify true moves of lawyers across firms. We limit the sample to lawyers who move among firms. Our estimating equations are a sequence as follows, with y_{ijt} being some compliance, monitoring or business development outcome for individual manager *i* in firm *j* at time *t*:

(*i*) $y_{ijt} = Firm\ \ fixed\ effects + Year\ \ fixed\ effects$

(*ii*) $y_{ijt} = Firm\ \ fixed\ effects + Year\ \ fixed\ effects + Lawyer\ \ fixed\ effects$

(*iii*) $y_{ijt} = Firm\ \ fixed\ effects + Year\ \ fixed\ effects + Lawyer\ \ fixed\ effects + CEO\ \ fixed\ effects$

The main inference from this method comes from calculating the increase in adjusted r-squared moving from equation (i) to (ii). Because a lawyer effect may be spuriously correlated with CEO effects, which the literature finds to be robustly important, we follow Ge et al. (2011) in including equation (iii) to test whether the economic and statistical significance of lawyer effects holds in the presence of CEO effects. One should take caution in interpreting the magnitude of CEO fixed effects in equation (iii) because we restrict the sample to general counsel movers but not CEO movers. We provide a better magnitude comparison in Appendix 2, which reports the CEO fixed effects estimation using a CEO mover sample.

IV.b. Importance of lawyers: Results

Table 2 reports the lawyer fixed effects results, mimicking the layout of Bertrand and Schoar (2003). The table reads down by rows, with the first row under each variable reporting the adjusted r-squared for a model of just firm and year fixed effects. For the compliance measures, these adjusted r-squareds for AAERs and insider trading are 0.512 and 0.208 respectively. The addition of a lawyer fixed effect (the second row) increases the r-squared to 0.528 and 0.262, representing an average improvement of 3.5 percentage points of variation explained (1.6 percentage points for AAERs and 5.4 percentage points in insider trading). The F-tests for the joint significance of the lawyer fixed effects have a p-values of <0.01. These result are robust to the addition of CEO fixed effect (the third row). In Appendix Table 2, we report that CEO fixed effects (using a CEO movers sample) explain 19.6 percentage points in compliance variation; thus, general counsels are slightly less than 20% as relevant as CEOs.

In terms of monitoring, the lawyer fixed effects explain 6.8 percentage of the variation in securities fraud, 4.9 percentage points of the variation in general lawsuits, and 18.1 percentage points of the variation in backdating. Overall, the lawyer fixed effects explain an average of 10 percentage points in monitoring outcomes variation. Compared to the CEO fixed effects reported in Appendix Table 2, the magnitude of lawyer fixed effect in monitoring represents 40% of the relevance of CEOs.

Finally, for the business development variables, the lawyer fixed effects explain 1.3 percentage points of the variation in capital expenditures and 5.3 percentage points of the variation in business

segments. Across these measures, the lawyer fixed effects explain an average of 3.3 percentage points in business development. Appendix Table 2 shows that CEOs explain an average of 6 percentage points, in this case, suggesting that general counsel are almost 60% as relevant as CEOs in organic growth. Neither lawyer nor CEO heterogeneity has power in explaining corporate innovation as measured by R&D, which is consistent with the findings of Cho, Halford, Hsu and Ng (2016).

It is worth pausing to consider the relative magnitudes of these finding. Compared against CEO effects, lawyer heterogeneities are much more important in monitoring and business development than they are in compliance. Our interpretations are twofold. First, individual lawyers may not be able to distinguish themselves in the compliance facet of governance because compliance is so important to all general counsel. Second, consistent with our ideas of lawyers facing tradeoffs in exerting their constrained time toward monitoring versus business development, individual lawyers may be able to distinguish themselves to be skilled in these dimensions.

IV.c. Importance of lawyers: Robustness methodology

Interpreting the lawyer fixed effects results with generalizable causality language could be problematic if lawyers that move among firms are mobile because of the individual's capability in compliance, monitoring, or business development. Thus, we implement a robustness approach that identifies off the decision of hiring executive lawyers. We ask whether firms that hire an ExecLawyer experience changes in compliance, monitoring, and business development that are different compared to those not hiring, using a propensity score matched difference-in-differences approach. This approach has endogeneity issues of its own: even after propensity matching firms on observables, unobservables such as the future need for an executive lawyer may determine the hiring decision. The sign of the bias should be conservative for compliance and monitoring: if a firm has a future need for governance, it is likely that the firm is entering a phase of increased pressure on their governance, thereby biasing downward any

positive effect of hiring an ExecLawyer on such outcomes[15]. Thus, even though this approach cannot be ascertained to be free of selection, it imposes an opposite selection compared to the previous methodology – looking at all hires compared to none (here) versus looking among heterogeneities within the hires and fires (the lawyer fixed effects method). Thus, if the two methods produce similar results, the inference is quite suggestive of causality.

Appendix Table 3 provides summary statistics that compare firms hiring an ExecLawyer (who stays for at least three years) to non-hiring firms (i.e., firms that do not have executive lawyers from two years prior to two years after). The firms differ in a few dimensions. For example, firms that hire ExecLawyer tend to have more incidences of compliance and monitoring failures, reflecting the need for gatekeeping. Further, they are smaller in market capitalization; have higher leverage and larger business segments but lower market-to-book, ROA, and R&D expenses. Thus, we match the treated firms that hire to control firms that do not hire in year of the hire and one-digit industry, and then within these matched buckets, we draw three nearest neighbor matches on the hiring propensity score gauged off variables capturing past and future needs for compliance, monitoring, and business development. Appendix Table 4 model (1) reports the fitting of the propensity logit model. Firms that hire external lawyers tend to have stronger needs for compliance and business development, largely consistent with Appendix Table 3.

IV.d. Importance of lawyers: Robustness results

Table 3 (Panel A) reports the robustness results speaking to the importance of ExecLawyers. For brevity, we only report the collapsed difference-in-differences results (the most stringent specification) of these robustness regressions (Bertrand, Duflo, and Mullainathan, 2004). The dependent variable is the change in outcome (compliance, monitoring or business development) from pre-hiring to post-hiring. Each firm has one observation, and estimation weights balance the matching. For example, in this

15 We cannot make this conservative claim for business development, and in fact our instincts are that the bias would likely be anticonservative. However, we include the results only for parallel reporting of results and transparency.

collapsed specification the AAERs dependent variable would be the occurrence of any AAER (the max over a 0-1 variable) in the two years following the hire, excluding the hiring year, minus the occurrence of any AAER in the two years prior to the hire year. Our sample comprises 513 firms hiring ExecLawyers and 784 matched non-hiring firms. Odd numbered columns are the raw difference-in-differences, and even columns include hire year and industry (two-digit SIC code) fixed effects.

We find that the two compliance failure measures are strongly significant (both economically and statistically) in the direction of the executive lawyer being a mechanism in improving compliance.[16] In terms of economic magnitude, the incidence of AAERs and insider trading in hiring firms is 4.6 percentage points and 2.4 percentage points lower, respectively, compared to control firms over the two-year period post hiring of ExecLawyer. Likewise, in Panel B, hiring firms exhibit fewer securities fraud incidents and general lawsuits, but not backdating. In monitoring dimension, securities fraud and general lawsuits are 3.9 and 4.8 less frequent over the two years post period respectively compared to control firms. The inference we are comfortable drawing from Table 3 is that executive lawyers are robustly important in compliance and monitoring.

We do not find any effect of hiring an executive lawyer on business development except for some weak evidence on business segments. We interpret any results with caution here because business development implies distinct tasks for different companies (e.g., oversight on patents for high tech companies, FDA approval for drug companies, branding for consumer product companies, etc.), making it difficult to pin down common measurements of executive lawyers' efforts in this role in this stringent setup.

Finally, we explore whether the hiring of ExecLawyers reflects an overall strategy implemented by boards or CEOs to improve governance on many dimensions. We look to other governance actions taken by the board or shareholders at the same time as hiring an executive lawyer and find no effects timed to the executive lawyer hiring.

[16] Our findings are consistent with Kwak, et al. (2012)'s and Jagolinzer, et al. (2011)'s studies which finds compliance improvements with the presence of super lawyers in the firm.

For consistency and robustness, we report the collapsed difference-in-difference estimation results for the external hiring of General Counsel (rather than top five paid ExecLawyer) in Panel B of Table 3. The dependent variable is the change in outcome variables from pre-hiring to post-hiring of General Counsel. Our results (in both statistical significance and economic magnitudes) are consistent with those presented in Panel A, providing further robustness evidence for the importance of lawyers on compliance and monitoring.

V. Gatekeepers versus Totems

V.a. Gatekeepers versus totems: Methodology

Our main agenda is to explore whether executive lawyers are induced to trade off gatekeeping when they have incentive contracts designed to reward business development efforts. Our identification novelty is a comparison across two sets of firms, both hiring executive lawyers. One set hires from law firms; the other, from other corporations. Our main identifying assumption is that executive lawyers hired from law firms are *initially* less likely to reduce their gatekeeping effort as a reaction to equity incentives than are executive lawyers poached from other corporations. We first motivate this source of hiring assumption and then lay out how we can use the source of hiring for a plausibly-causal identification.

Executives that are hired from law firms have built both their human capital and their reputational capital in lawyering not corporate strategic decision-making. These lawyers have rarely worked outside law firms. By training and by practice, gatekeeping comes more naturally than risk-taking, reinforced by the conservative biases of law practice and by the reality that the newly-hired law firm lawyer has all of her reputation at stake in the event of a gatekeeping failure. Once inside the firm, the sociology literature on professionalism guides our thinking about the transformation of lawyers with professional identities. Goode (1957) defines a professional community (e.g., doctors, lawyers, professors, etc.) as occupations where all members are bounded by a sense of identity and common values. Hall (1968) documents that professionals working inside an organization may identify less with the organization compared to other employees, because of conflicts between administrative imperatives and professional norms. Consistent

with our assumption most directly, Wallace (1995) finds that lawyers working in corporations are significantly less committed to the legal profession than those working in law firms.

Putting these ideas together, law firm lawyers (i) exhibit loyalty to their professional association, (ii) must go through a learning curve to understand the business development strategy of the firm, (iii) must change their trained risk-aversion habit as a lawyer and learn to be more comfortable with risk, and (iv) must be willing to step away from their stock of reputational capital. All of these factors imply that law firm-hired lawyers should be less likely on average than corporate-hired lawyers to respond to equity incentives in such a way as trading off gatekeeping for strategic input.

Our comparison of the effect of equity incentives on law firm hired-lawyers versus corporate hired-lawyers does not presume that corporations exogenously choose the source of hiring. Our design in this section begins by levelling firms on the ex ante propensity to select one hiring source over the other and then absorbs any ex post outcome differences induced by the hiring source. Below we lay out these details, and the exogeneity assumption that we need.

Our estimating equation for our main test on equity incentives is as follows:

$$\begin{aligned} y_{it} &= \alpha_1 Post_{it} + \alpha_2 CorporateHire_i + \alpha_3 Post_{it} CorporateHire_i + \mu_{year} + \mu_{industry} + \mu_{hireyear} \\ &+ \alpha_4 ExecLawyerDelta_{i,hireyear} + \alpha_5 CorporateHire_i ExecLawyerDelta_{i,hireyear} \\ &+ \alpha_6 Post_{it} ExecLawyerDelta_{i,hireyear} + \alpha_7 Post_{it} CorporateHire_i ExecLawyerDelta_{i,hireyear} + \varepsilon_{it} \end{aligned} \quad (1)$$

y_{it} is the outcome measure of compliance, monitoring, or business development. $Post_{it}$ is an indicator being equal to zero for the two years before a hire and one for the two years following the hire, excluding the hire year. (Our results hold extending the ex post duration to three years.) The sample is firms that hire an ExecLawyer externally from either another company (treatment group: *CorporateHire*=1) or a law firm (control group: *CorporateHire*=0). $ExecLawyerDelta_{i,hireyear}$ is the compensation delta of the ExecLawyer *i*, defined only at the hiring year to avoid confounding effect of performance. The delta primarily captures sign-on incentive contracting. Although $ExecLawyerDelta_{i,hireyear}$ is in the future for the *Post = 0* observations, its interaction with *CorporateHire* allows us to difference out a selection

effect. (Our results hold if we remove this level effect.) Our variable of interest is α_7, the coefficient on the difference-in-differences term interacted with the compensation delta $Post_{it}CorporateHire_i ExecLawyerDelta_{i,hireyear}$.

Before we estimate equation (1), we propensity-score match firms to deal with ex ante selection of hiring from a corporation versus a law firm. Our propensity score matching procedure first double sorts firms into one-digit industry and hire year buckets and then selects three nearest neighbor matches on the likelihood of a firm hiring from a law firm as opposed to from a corporation, using the variables capturing current or future need for compliance, monitoring or business development (as in Section IV.c). Appendix Table 4 model (2) reports the results of the logit propensity formulation. Appendix Table 5 compares firm and executive statistics in the year of hiring for the corporate hire firms and the law firm hire firms after matching, finding no statistically significant differences by hiring source.

It could be that the source of hiring is still endogenous to ex post outcomes. However, our inference comes not from a difference-in-differences estimator but from the difference-in-difference estimator interacted with delta. That is, we only interpret $Post_{it}CorporateHire_i$ as absorbing any ex post selection in hiring from the corporation. De facto, however, after propensity-score matching and differencing, we find little-to-no evidence for any ex ante or ex post selection by hiring source.

Our identification does rely, however, on one exogeneity condition for interpreting our main variable of interest, α_7: Had the firm hired an ExecLawyer from a corporation, the firm's outcome sensitivity to equity incentives would have evolved similarly as had they hired from a law firm, once we propensity match, control for both the ex-ante and ex post selection of hiring from a corporation (*CorporateHire, Post, and Post*CorporateHire*), and control for selection on any incentive pay needs of the firm ($ExecLawyerDelta_{i,hireyear}$, $CorporateHire_i ExecLawyerDelta_{i,hireyear}$). With so many differencing and interactions, it is perhaps easier to state the opposite – what it would take for our identification to fail. It could be that the firm's selection of hiring sources may reflect some omitted variable correlated with the effectiveness of equity incentives. That is, it is possible that some unobservable factor could drive both

the selection of hiring sources and the sensitivity of corporate outcomes to equity incentives. To address this concern, we implement a triple difference form as follows:

$$\begin{aligned} y_{it} &= \alpha_1 Post_{it} + \alpha_2 CorporateHire_i + \alpha_3 Post_{it} CorporateHire_i + \mu_{year} + \mu_{industry} + \mu_{hireyear} \\ &+ \alpha_4 ExecLawyerDelta_{i,hireyear} + \alpha_5 CorporateHire_i ExecLawyerDelta_{i,hireyear} \\ &+ \alpha_6 Post_{it} ExecLawyerDelta_{i,hireyear} + \alpha_7 Post_{it} CorporateHire_i ExecLawyerDelta_{i,hireyear} \\ &+ \alpha_8 Post_{it} CEODelta_{i,hireyear} + \alpha_9 Post_{it} CorporateHire_i CEODelta_{i,hireyear} + \varepsilon_{it} \end{aligned} \quad (2)$$

We introduce $CEODelta_{i,hireyear}$ into the equation, which is the level of equity incentives of the CEO in the hiring year of the ExecLawyer. In essence, we are forcing the comparison to difference around the endogenous use of equity incentives for firms. Contract theory predicts that firms with different contracting environment vary in optimal incentive levels. Studies on executive compensation (e.g. Core, Holthausen and Larcker (1999), Armstrong, Jagolinzer, and Larcker (2010)) suggest that both innate firm economic characteristics such as size, complexity, growth, and firm corporate governance characteristics affect managerial compensation. $CEODelta_{i,hireyear}$ should capture the unobservable differences in compensation contracting environment between the treatment group and matched firms, if there are any.

To deal with the concerns of serial correlation and over-rejection of the null, we adopt as robustness the collapsed estimation procedure recommended by Bertrand, Duflo, and Mullainathan (2004). We collapse our time series observation around ExecLawyer hiring into pre and post periods and calculate the change in outcome measures of the treatment group and the control group respectively. The form of this estimation equation is given below, where Δ implies the average in the post period minus the average in the pre period:

$$\begin{aligned} \Delta y_t &= \lambda_1 CorporateHire_i + \lambda_2 ExecLawyerDelta_{i,hireyear} + \lambda_3 CorporateHire_i ExecLawyerDelta_{i,hireyear} \\ &+ \lambda_4 CEODelta_{i,hireyear} + \lambda_5 CorporateHire_i CEODelta_{i,hireyear} + \mu_{industry} + \mu_{hireyear} + \varepsilon_i \end{aligned} \quad (3)$$

V.b. Gatekeepers versus totems: Compliance results

Table 4 reports the double and triple differencing results as to whether equity incentives impact executive lawyers' effort exerted in regulatory compliance. Columns (1) to (3) consider AAER fraud

outcomes, and columns (4) to (6), SEC alleged insider trading. In columns (1) and (4), we find no difference in ex post compliance by hiring source. The main variable of interest in Table 4 is *Post*CorporateHire*Log(ExecLawyerDelta)*, where we have added $10,000 to the delta before taking the natural logarithm transformation so that we do not simply identify off the skewness. Columns (3) and (6) add in the further differencing around the equity incentive level of the CEO. We include a series of fixed effects for industry, year and hiring year, and cluster errors at the firm-hire level. Overall, we have 416 firm-hires which result in about four times that number of observations.

We find little evidence that equity incentives divert or enhance regulatory compliance efforts, as manifested in either AAER fraud or insider trading. The coefficient of interest is insignificant across all columns. The lack of an effect of incentive pay on compliance outcomes is perhaps to be expected because of steep reputation costs to infractions (Desai, Hogan, and Wilkins, 2006; Karpoff, Lee, and Martin, 2008).[17] Likewise, CEO deltas play no role in compliance outcomes in this setup.

V.c. Gatekeepers versus totems: Monitoring results

Table 5 repeats the exercise of Table 4, but this time for the monitoring aspect of gatekeeping. We measure monitoring effectiveness in three dimensions – securities frauds, general lawsuits, and option backdating. The sample is thinner for option backdating because backdating investigation stops in 2007. Again, we first start by looking at selection gauged ex post and find no evidence that the hiring source predicts different firm monitoring outcomes. The coefficients on *Post*CorporateHire* in columns (1) (securities fraud), (4) (general lawsuits) and (7) (backdating) are insignificant.

Turning to the main results, the coefficients on *Post*CorporateHire*Log(ExecLawyerDelta)* in columns (2), (3), (5), and (6) are all positive and significant. Under our plausibly-causal design interpretation, the optimal contracting of lawyers into strategic initiatives diverts lawyer time in

[17] In the monitoring results to be presented in the next section, we include robustness tables, limiting to only positive executive lawyer delta firms and implementing a collapsed version as well. For compliance, we find no results in these alternative specifications as well, and thus omit them for space considerations.

monitoring, resulting in an increase in the likelihood of a firm committing a monitoring breach. We find no impact on backdating outcomes, however.

In the prior table, we showed that CEO equity incentives were not associated with the probabilities of compliance failures. In Table 5, however, CEO incentives are positively associated with securities fraud, consistent with the literature (Wang, Winton and Yu, 2010). This effect is weaker in the general lawsuits specification and we make no claim that such an estimate is well-specified in our estimation framework, but the result is reassuringly in the right direction of what one might expect. Furthermore, for our purposes, lack of significance on the difference-in-differences interacted with CEO delta is reassuring that our matching across hiring source of ExecLawyers does not correlate with an omitted variable related to both the hiring source and the sensitivity of corporate outcomes to equity incentives.

In terms of the magnitude, we focus on a one standard deviation higher value of the *Log(ExecLawyerDelta)* in the cross section at the hiring year, or an equivalent $22,000 increase in *ExecLawyerDelta* above the mean value. These same lawyers hired with a $22,000 larger delta at sign-on have an approximately $60,000 delta two years post-hiring, which is perhaps the more appropriate way to state the comparison. After combining with the log transform and the bulk of zeros from the interaction terms *Post* and *CorporateHire*[18], we calculate that a one standard deviation larger *Log(ExecLawyerDelta)* increases the probability of securities law suits by 0.013. This marginal effect represents a percentage increase in class actions by 27.8% (shown at the bottom of Table 5). Our preferred way to interpret these results is as a percentage of the governance improvements associated with hiring an ExecLawyer from Table 3. In particular, when a corporation contracts an ExecLawyer with a one standard deviation higher sign-on equity incentive contract, it is diverting 67% of the prevention of securities litigation found in Table 3. For the general lawsuits, a one standard deviation higher value of the *Log(ExecLawyerDelta)*

[18] Alternatively, a one standard deviation increase in *Post*CorporateHire*Log(ExecLawyerDelta)* is more than two-times larger.

translates into an increase in the probability of general lawsuits by 0.012, an unwinding of 48.1% of the governance improvements in avoiding these lawsuits.

Before accepting these magnitude interpretations, we need to consider robustness of these results. We implement two more stringent specifications: (i) a specification when we focus on only those lawyers who are hired with positive delta, and (ii) a collapsed specifications per Bertrand, Duflo, and Mullanathan (2004).

Table 6 limits our sample to ExecLawyer hires with positive compensation delta only, eliminating lawyers with no sign-on equity incentives. Even though the number of observations drops by 40%, the coefficient estimates on the variable of interest *Post*CorporateHire*Log(ExecLawyerDelta)* hardly change in our new specification. With our sample limited to positive delta, a one standard deviation higher value of the *Log(ExecLawyerDelta*), i.e., a $38,000 increase in ExecLawyerDelta above the mean value, translates into an unwinding of 87.5% of the governance improvements in avoiding securities lawsuits and an unwinding of 71.9% of the governance improvements in avoiding general lawsuits. These magnitudes are naturally biased up relative to the full sample, in that ExecLawyers with no equity incentives dropped from the sample are likely to be gatekeepers.

Finally, Table 7 presents our most stringent specification in implementing a collapsed version of the difference in differences as in equation (3). The dependent variable is the change of governance measures from pre-hiring to post-hiring, thus each firm has one observation. Our variable of interest is *CorporateHire*Log(ExecLawyerDelta)*. As in the prior tables, the coefficient on this variable is positive and significant for securities fraud and general lawsuits. In terms of the magnitude, the value of governance reduction given one standard deviation change of *Log(ExecLawyerDelta)* for both securities lawsuits and general lawsuits is reassuringly in-between the economic effect given in Tables 5 and 6.

V.d. Gatekeepers versus totems: Business Development results

Table 8 reports the triple-difference specifications testing whether a firm's contracting with equity incentives impacts executive lawyers' effort exerted in business development. As before, we first

present a non-interacted specification in columns (1), (4), and (7) to test whether ex post business development outcomes differ by hiring source. We find no evidence for this selection. In columns (2), (5) and (8), we present the triple interaction results for capital expenditure, R&D and business segment dependent variables respectively. We omit the double differencing for brevity because the results look very similar to the triple differencing. In columns (3), (6), and (9), we report results for the sample dropping ExecLawyers with zero sign-on equity incentives.

We find some, albeit noisy, evidence consistent with our intuition that equity incentives should be associated with a firm contracting the ExecLawyer for business development. In column (2), the difference-in-differences coefficient interacted with equity incentives is a positive and significant 0.089. Firms that hire ExecLawyers from other corporations and provide them with a one standard deviation higher sign-on equity incentive packages exhibit 0.017 more capital expenditures-to-fixed assets in the coming two years, relative to those firms hiring from law firms. The coefficient in column (3) is similar to that for column (2), but the estimate is noisier with the smaller sample. In columns (5) and (6), we find that likewise, equity incentives for ExecLawyers have implications for R&D going forward, although this is only true for those with non-zero sign-on incentive contracts. Firms that hire ExecLawyers poached from other corporations and give them higher sign-on equity incentive package exhibit 0.005 R&D expenditures-to-assets in the coming two years, relative to those firms hiring from law firms with positive incentive deltas. We find no effects in business segments.

We want to exert some caution in interpreting these business development results for a number of reasons. First, the results become even less precisely estimated in a collapsed specification, which we omit from the tables for brevity. Second, in Table 3, we found no robust evidence for business development expansion when firms hire an ExecLawyer. Thus, although we see that ExecLawyer heterogeneities do matter for business development in the fixed effects analysis, our design is really aimed to identify the gatekeeping aspect of the tradeoff. Nevertheless, the evidence in Table 8 is consistent in the direction of the tradeoff we have in mind that firms make.

VI. Conclusion

Internal governance is an idea that has grown in popularity among executives, as they have increasingly become exposed to regulation and punishment for misconduct. In this paper, we have documented the importance of executive lawyers, arguably the most significant emblem of internal governance, to the firm in their multiple tasks: regulatory compliance, monitoring, and business development. Prior literature guides our intuition that individual executives matter (Bertrand and Schoar, 2003; Malmendier and Tate, 2009). Recently, Custodio and Metzger (2014) document that financial expertise matters inside the firm. We introduce legal expertise into the box, documenting that general counsels command meaningfully large governance and business development fixed effects. The work on the importance of external lawyers on M&A negotiations and outcomes by Krishnan and Masulis (2013) and Karsten, Malmendier and Sautner (2014) is a nice complement and also serves this motivating purpose.

For our purposes, however, gatekeeping and strategic advisory roles of lawyers in executive offices together imply a tension of time allocation. We offer evidence that executive lawyers are incentivized to compromise internal governance monitoring time when faced with the call to add strategic input; they do not, however, compromise regulatory compliance, implying that these executive lawyers on average remain gatekeepers, at least in some dimensions, even though corporations use their intellectual property expertise and other legal expertise in business development planning.

Coffee (2002) might fairly interpret our results that compensation distorts gatekeeping. Surely it is difficult to reconcile the duties of an executive agent (Berle and Means, 1932) with those of a reputation intermediary positioned by owners to prevent managerial wrongdoing (Coffee, 2006). We have taken a view more in line with optimal contracting, because legal expertise seems increasingly valuable in strategic decisions in our information economy. We conclude with the thought that as long as intellectual property continues to be a major part of production, legal expertise will continue to be needed in decision making, and the lines between legal value-creators and legal guardians will remain blurry. Intellectual property is not going away.

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Table 1: General Counsel and Executive Lawyer Characteristics over Time

This table presents General Counsel (GC) and Executive Lawyer (ExecLawyer) characteristics (mean) by fiscal year. Our sample comprises firm years in ExecuComp from 1995 to 2012. Statistics reported in (1)-(3) are for the whole sample while statistics reported in (4)-(9) are for firm years with the presence of ExecLawyer. ExecLawyer is an indicator variable equal to one if a general counsel appears in ExecuComp as one of the top paid executives. ExecLawyer pay is the executive lawyer's total compensation (salary, bonus, other cash compensation, option grants, and restricted stocks) in constant 2012 dollars. CEO pay is the CEO's total compensation. ExecLawyer delta is the executive lawyer's total wealth to performance sensitivities based on stock holdings and unexercised options in constant 2012 (million) dollars, following Core and Guay (1999). CEO delta is the CEO's total wealth to performance sensitivities based on stock holdings and unexercised options in constant 2012 (million) dollars.

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Year	# of firm years	Firms with GC as corporate officer	Firms with Exec-Lawyer	Exec-Lawyer Age	Exec-Lawyer pay	CEO pay	Exec-Lawyer pay / CEO pay	Exec-Lawyer delta	CEO delta
1995	1,727	0.664	0.328	49.3	1,032	4,550	0.344	0.025	0.516
1996	1,926	0.648	0.320	49.5	1,351	6,716	0.364	0.034	0.653
1997	1,993	0.656	0.330	49.5	1,477	8,289	0.353	0.044	0.898
1998	2,030	0.668	0.353	49.7	1,600	12,523	0.335	0.047	0.933
1999	1,928	0.679	0.377	49.9	1,964	10,007	0.381	0.068	1.351
2000	1,831	0.707	0.398	50.1	2,088	11,067	0.346	0.064	1.247
2001	1,786	0.713	0.411	50.4	1,747	9,155	0.353	0.048	0.995
2002	1,821	0.714	0.426	50.6	1,436	6,740	0.369	0.041	0.821
2003	1,866	0.714	0.429	50.8	1,547	7,021	0.335	0.057	0.947
2004	1,810	0.731	0.408	51.1	1,567	7,403	0.345	0.068	0.789
2005	1,697	0.745	0.357	51.8	1,841	7,651	0.358	0.085	0.921
2006	1,858	0.747	0.377	51.3	1,196	4,793	0.416	0.097	1.279
2007	1,857	0.753	0.395	51.2	1,175	4,102	0.442	0.066	1.017
2008	1,790	0.765	0.410	51.2	973	3,359	0.414	0.039	0.509
2009	1,727	0.776	0.412	51.5	1,350	4,940	0.398	0.046	0.507
2010	1,666	0.794	0.466	52.0	1,133	4,034	0.394	0.049	0.603
2011	1,593	0.804	0.466	52.4	982	3,568	0.402	0.047	0.705
2012	1,466	0.808	0.440	53.3	1,537	3,355	0.431	0.059	0.852
All	32,372	0.724	0.393	50.9	1,445	6,580	0.378	0.055	0.865

Table 2: General Counsel Fixed Effects Estimates of Compliance, Monitoring and Business Development Using General Counsel Movers

This table presents the general counsel fixed effects, 1995-2012. Each row represents a regression for the dependent variable to the left. The sample is limited to firm-year observations covering general counsel movers. The fixed effects included are: year and firm fixed effects in row 1; year, firm, andgeneral counsel fixed effects in row 2; year, firm, CEO, and general counsel fixed effects in row 3. Reported in the second and third columns are F-tests for the joint significance of the CEO fixed effects and general counsel fixed effects. For each F-test, we report the value of the F-statistic, the p-value, and the number of constraints.The final two columns report the adjusted R-squared and the partial adjusted r-square for general counsel. *AAER Fraud* is an indicator for a restatement investigation by the SEC covering the observation year. *SEC Insider Trading* is an indicator for an executive being investigated for insider trading by the SEC. *Securities Fraud* is an indicator that takes on the value of one for fiscal years coinciding with the class period identified by the securities class action lawsuits. *General Lawsuits* is an indicator for fiscal years coinciding with the class period for any lawsuit (e.g. breach of any law, including security law, energy law, international law, employment law, etc.) with positive settlement amount. *Backdating* is an indicator for firm years for which firms are convicted of backdating or misdating. *CapEx* is the ratio of capital expediture to PP&E measured at the beginning of the fiscal year. *R&D* is the R&D expenses scaled by assets at the beginning of the fiscal year. *Business segments* are in counts of business lines, capturing complexity.

	F-tests on fixed effects for				
	General Counsels	CEOs	N	Adjusted R-squared	General Counsel Partial R-squared
Compliance Failures					
AAER Fraud			2,536	0.512	
	1.28*** (.0076, 205)		2,536	0.528	0.016
	0.70 (.9950, 133)	2.81*** (<.0001, 262)	2,536	0.622	
SEC Insider Trading			3,172	0.208	
	1.69*** (<.0001, 238)		3,172	0.262	0.054
	1.94*** (<.0001, 149)	1.66*** (<.0001, 340)	3,172	0.297	
Monitoring Failures					
Securities Fraud			3,172	0.351	
	2.10*** (<.0001, 238)		3,172	0.419	0.068
	2.18*** (<.0001, 149)	2.63*** (<.0001, 340)	3,172	0.518	
General Lawsuits			3,172	0.590	
	2.27*** (<.0001, 238)		3,172	0.639	0.049
	2.32*** (<.0001, 149)	2.78*** (<.0001, 340)	3,172	0.700	
Backdating			2,155	0.276	
	3.47*** (<.0001, 171)		2,155	0.457	0.181
	2.87*** (<.0001, 100)	2.89*** (<.0001, 212)	2,155	0.481	
Business Development					
Capex			3,090	0.682	
	1.39*** (<.0001, 231)		3,090	0.695	0.013
	1.97*** (<.0001, 145)	3.25*** (<.0001, 333)	3,090	0.776	
R&D			2,120	0.340	
	1.32 (1.0000, 235)		2,120	0.288	-
	0.32 (1.0000, 148)	0.36 (1.0000, 336)	2,120	0.230	
Business segments			3,172	0.752	
	3.54*** (<.0001, 238)		3,172	0.805	0.053
	2.37*** (<.0001, 149)	3.01*** (<.0001, 340)	3,172	0.838	

Table 3: Collapsed Difference-in-Differences Test for the Importance of ExecLawyers and General Counsel

This table presents the collapsed difference-in-differences tests around the external hiring of Execlawyer (Panel A) and General Counsel (Panel B). The dependent variable is the change of compliance, monitoring or business development measures from pre-hiring to post-hiring, thus each firm has one observation. The treatment group is corporations hiring ExecLawyers, and the control group is non-hirng firms that are matched within the year-industry-size and by the propensity score of hiring an ExecLawyer. Post is set to zero for the two years prior to the hiring of ExecLawyer, and one for the two years subsequent. The year of hiring is tossed out. *AAER Fraud* is an indicator for a restatement investigation by the SEC covering the observation year. *SEC Insider Trading* is an indicator for an executive being investigated for insider trading by the SEC. *Securities Fraud* is an indicator that takes on the value of one for fiscal years coinciding with the class period identified by the securities class action lawsuits. *General Lawsuits* is an indicator for fiscal years coinciding with the class period for any lawsuit (e.g. breach of any law, including security law, energy law, international law, employment law, etc.) with positive settlement amount. *Backdating* is an indicator for firm years for which firms are convicted of backdating or misdating. *CapEx* is the ratio of capital expediture to PP&E measured at the beginning of the fiscal year. *R&D* is the R&D expenses scaled by assets at the beginning of the fiscal year. *Business segments* are in counts of business lines, capturing complexity. *Board independence* is the percentage of independent directors on board. *Governance index* is the Gompers, Ishii and Metrick (2003) governance index. Our sample comprises firm years in ExecuComp from 1995 to 2012. Standard errors are clustered at the firm level. Superscripts ***, **, * indicate statistical significance level at the 1%, 5%, and 10% level, respectively.

Panel A: ExecLawyer

Compliance Failures	(1)	(2)	(3)	(4)		
	AAER Fraud	AAER Fraud	SEC Insider Trading	SEC Insider Trading		
ExecLawyer Hiring	-0.040***	-0.046***	-0.026***	-0.024***		
	[0.015]	[0.016]	[0.009]	[0.009]		
Hire Year and SIC 2-Digit F.E.	N	Y	N	Y		
Observations	1,079	1,079	1,316	1,316		
R-squared	0.007	0.077	0.007	0.097		
Monitoring Failures	(1)	(2)	(3)	(4)	(5)	(6)
	Securities Fraud	Securities Fraud	General Lawsuits	General Lawsuits	Backdating	Backdating
ExecLawyer Hiring	-0.040**	-0.039**	-0.053***	-0.048**	0.002	0.005
	[0.016]	[0.018]	[0.018]	[0.019]	[0.008]	[0.007]
Hire Year and SIC 2-Digit F.E.	N	Y	N	Y	N	Y
Observations	1,316	1,316	1,316	1,316	835	835
R-squared	0.004	0.068	0.007	0.07	0.000	0.116
Business Development	(1)	(2)	(3)	(4)	(5)	(6)
	Capex	Capex	R&D	R&D	Business Segments	Business Segments
ExecLawyer Hiring	-0.023	-0.013	0.000	-0.001	0.279*	0.038
	[0.022]	[0.026]	[0.005]	[0.004]	[0.164]	[0.150]
Hire Year and SIC 2-Digit F.E.	N	Y	N	Y	N	Y
Observations	1,324	1,324	1,288	1,288	1,316	1,316
R-squared	0.001	0.115	0.000	0.142	0.002	0.264
Other Governance	(1)	(2)	(3)	(4)		
	Board Independence	Board Independence	Governance Index	Governance Index		
ExecLawyer Hiring	0.896	0.822	0.068	0.08		
	[0.599]	[0.604]	[0.063]	[0.067]		
Hire Year and SIC 2-Digit F.E.	N	Y	N	Y		
Observations	1,056	1,056	652	652		
R-squared	0.002	0.122	0.002	0.14		

Panel B: General Counsel

Compliance Failures	(1)	(2)	(3)	(4)		
	AAER Fraud	AAER Fraud	SEC Insider Trading	SEC Insider Trading		
General Counsel Hiring	-0.022	-0.034*	-0.028**	-0.027**		
	[0.015]	[0.018]	[0.012]	[0.013]		
Hire Year and SIC 2-Digit F.E.	N	Y	N	Y		
Observations	647	647	744	744		
R-squared	0.003	0.116	0.007	0.071		
Monitoring Failures	(1)	(2)	(3)	(4)	(5)	(6)
	Securities Fraud	Securities Fraud	General Lawsuits	General Lawsuits	Backdating	Backdating
General Counsel Hiring	-0.050**	-0.053**	-0.054**	-0.055**	0.004	0.000
	[0.022]	[0.023]	[0.022]	[0.023]	[0.015]	[0.014]
Hire Year and SIC 2-Digit F.E.	N	Y	N	Y	N	Y
Observations	744	744	744	744	546	546
R-squared	0.007	0.118	0.008	0.152	0.000	0.139
Business Development	(1)	(2)	(3)	(4)	(5)	(6)
	Capex	Capex	R&D	R&D	Business Segments	Business Segments
General Counsel Hiring	0.01	-0.005	-0.013	-0.017	0.632***	0.515***
	[0.032]	[0.028]	[0.011]	[0.011]	[0.185]	[0.173]
Hire Year and SIC 2-Digit F.E.	N	Y	N	Y	N	Y
Observations	743	743	725	725	744	744
R-squared	0.000	0.177	0.002	0.097	0.015	0.329
Other Governance	(1)	(2)	(3)	(4)		
	Board Independence	Board Independence	Governance Index	Governance Index		
General Counsel Hiring	-0.295	-0.017	-0.02	-0.046		
	[0.919]	[0.981]	[0.088]	[0.101]		
Hire Year and SIC 2-Digit F.E.	N	Y	N	Y		
Observations	585	585	377	377		
R-squared	0.000	0.154	0.000	0.207		

Table 4: The Effect of ExecLawyer Equity Incentives on Compliance

This table presents double and triple differencing estimations of the effect of ExecLawyer incentive pay on compliance failures, 1995-2012. The treatment group is corporations hiring ExecLawyers from other corporations, and the control group is firms that hire ExecLawyers from law firms, matched within the year-industry-size and by the propensity score of hiring from law firms vs. corporations. Post is set to zero for the two years prior to the hiring of ExecLawyer, and one for the two years subsequent. The year of hiring is tossed out. CEO delta and ExecLawyer delta are the respective manager's total wealth to performance sensitivities based on stock holdings and unexercised options in constant 2012 (million) dollars, following Core and Guay (1999). *AAER Fraud* is an indicator for a restatement investigation by the SEC covering the observation year. *SEC Insider Trading* is an indicator for an executive being investigated for insider trading by the SEC.Standard errors are clustered at the firm level. Superscripts ***, **, * indicate statistical significance level at the 1%, 5%, and 10% level, respectively.

	(1) AAER Fraud	(2) AAER Fraud	(3) AAER Fraud	(4) SEC Insider Trading	(5) SEC Insider Trading	(6) SEC Insider Trading
Post	0.021	0.072	0.071	-0.024*	-0.072**	-0.070**
	[0.038]	[0.089]	[0.102]	[0.013]	[0.036]	[0.034]
CorporateHire	-0.012	-0.143	-0.143	-0.02	-0.059	-0.059
	[0.024]	[0.111]	[0.110]	[0.014]	[0.043]	[0.043]
Post*CorporateHire	0.009	0.094	0.097	0.018	0.059	0.064
	[0.028]	[0.133]	[0.145]	[0.014]	[0.041]	[0.041]
Log(ExecLawyerDelta)		0.015	0.015		-0.021*	-0.021*
		[0.018]	[0.018]		[0.011]	[0.011]
Post*Log(ExecLawyerDelta)		-0.025	-0.026		0.018*	0.019*
		[0.025]	[0.023]		[0.010]	[0.011]
CorporateHire*Log(ExecLawyerDelta)		0.049	0.049		0.014	0.014
		[0.045]	[0.045]		[0.011]	[0.011]
Post*CorporateHire*Log(ExecLawyerDelta)		**-0.033**	**-0.033**		**-0.015**	**-0.013**
		[0.052]	**[0.051]**		**[0.011]**	**[0.011]**
Post*Log(CEODelta)			0.000			-0.001
			[0.008]			[0.001]
Post*CorporateHire*Log(CEODelta)			-0.001			-0.002
			[0.010]			[0.002]
Hire Year F.E.	Y	Y	Y	Y	Y	Y
Calendar Year F.E.	Y	Y	Y	Y	Y	Y
SIC Two-Digit F.E.	Y	Y	Y	Y	Y	Y
Observations	1,357	1,357	1,357	1,650	1,650	1,650
R-squared	0.100	0.111	0.111	0.066	0.071	0.071

Table 5: The Effect of ExecLawyer Equity Incentives on Monitoring

This table presents double and triple differencing estimations of the effect of ExecLawyer incentive pay on monitoring failures, 1995-2012. The treatment group is corporations hiring ExecLawyers from other corporations, and the control group is firms that hire ExecLawyers from law firms, matched within the year-industry-size and by the propensity score of hiring from law firms vs. corporations. Post is set to zero for the two years prior to the hiring of ExecLawyer, and one for the two years subsequent. The year of hiring is tossed out. CEO delta and ExecLawyer delta are the respective manager's total wealth to performance sensitivities based on stock holdings and unexercised options in constant 2012 (million) dollars, following Core and Guay (1999). *Securities Fraud* is an indicator that takes on the value of one for fiscal years coinciding with the class period identified by the securities class action lawsuits. *General Lawsuits* is an indicator for fiscal years coinciding with the class period for any lawsuit (e.g. breach of any law, including security law, energy law, international law, employment law, etc.) with positive settlement amount. *Backdating* is an indicator for firm years for which firms are convicted of backdating or misdating. Governance reduction for a standard deviation change in ExecLawyer delta in the hiring year is presented at the bottom of the table. It is then compared to the pre-hiring mean of the governance failure measure (Appendix Table 3) to calculate reduction percentage. Reduction as a percentage of governance improvement is the ratio of governance reduction to governance improvement (Table 3). Standard errors are clustered at the firm level. Superscripts ***, **, * indicate statistical significance level at the 1%, 5%, and 10% level, respectively.

	(1) Securities Fraud	(2) Securities Fraud	(3) Securities Fraud	(4) General Lawsuits	(5) General Lawsuits	(6) General Lawsuits	(7) Back-dating	(8) Back-dating	(9) Back-dating
Post	0.021	0.123	0.036	0.031	0.106	0.03	0.009	0.056	0.036
	[0.037]	[0.092]	[0.115]	[0.037]	[0.092]	[0.116]	[0.015]	[0.065]	[0.060]
CorporateHire	-0.041**	-0.056	-0.05	-0.046*	0.013	0.017	-0.012	0.149	0.152
	[0.020]	[0.067]	[0.067]	[0.026]	[0.104]	[0.105]	[0.020]	[0.104]	[0.104]
Post*CorporateHire	0.003	-0.185*	-0.096	-0.002	-0.167*	-0.111	-0.01	-0.085	-0.08
	[0.028]	[0.095]	[0.113]	[0.031]	[0.100]	[0.124]	[0.009]	[0.065]	[0.073]
Log(ExecLawyerDelta)		-0.018	-0.016		0.017	0.02		0.048	0.05
		[0.019]	[0.019]		[0.038]	[0.037]		[0.033]	[0.033]
Post*Log(ExecLawyerDelta)		-0.037	-0.055**		-0.027	-0.044		-0.019	-0.023
		[0.025]	[0.027]		[0.026]	[0.028]		[0.024]	[0.025]
CorporateHire*Log(ExecLawyerDelta)		0.005	0.003		-0.021	-0.023		-0.062	-0.063
		[0.020]	[0.021]		[0.036]	[0.037]		[0.039]	[0.039]
Post*Corporate*Log(ExecLawyerDelta)		**0.069****	**0.084****		**0.061***	**0.069****		**0.030**	**0.031**
		[0.030]	**[0.032]**		**[0.032]**	**[0.035]**		**[0.026]**	**[0.026]**
Post*Log(CEODelta)			0.026*			0.023			0.006
			[0.015]			[0.015]			[0.007]
Post*CorporateHire*Log(CEODelta)			-0.024			-0.015			-0.001
			[0.016]			[0.020]			[0.009]
Hire Year F.E.	Y	Y	Y	Y	Y	Y	Y	Y	Y
Calendar Year F.E.	Y	Y	Y	Y	Y	Y	Y	Y	Y
SIC Two-Digit F.E.	Y	Y	Y	Y	Y	Y	Y	Y	Y
Observations	1,650	1,650	1,650	1,650	1,650	1,650	1,076	1,076	1,076
R-squared	0.100	0.110	0.117	0.115	0.117	0.122	0.108	0.122	0.124
Pre-Hire Mean		*0.047*	*0.047*		*0.085*	*0.085*			
Given a one standard deviation increase in Log(ExecLawyerDelta):									
Magnitude of governance improvement		*0.020*	*0.020*		*0.024*	*0.024*			
Governance reduction (in % points)		*0.013*	*0.016*		*0.012*	*0.013*			
Governance reduction (in % change) given		*27.8%*	*33.8%*		*13.5%*	*15.3%*			
Reduction as % of governance improvement		*67.0%*	*81.5%*		*48.1%*	*54.4%*			

Table 6: The Effect of ExecLawyer Equity Incentives on Monitoring - Keeping Only Non-Zero ExecLawyer Delta

This table presents double and triple differencing estimations of the effect of ExecLawyer incentive pay on monitoring failures after removing observations with zero ExecLawyerDelta, 1995-2012. The treatment group is corporations hiring ExecLawyers from other corporations, and the control group is firms that hire ExecLawyers from law firms, matched within the year-industry-size and by the propensity score of hiring from law firms vs. corporations. Post is set to zero for the two years prior to the hiring of ExecLawyer, and one for the two years subsequent. The year of hiring is tossed out. CEO delta and ExecLawyer delta are the respective manager's total wealth to performance sensitivities based on stock holdings and unexercised options in constant 2012 (million) dollars, following Core and Guay (1999). *Securities Fraud* is an indicator that takes on the value of one for fiscal years coinciding with the class period identified by the securities class action lawsuits. *General Lawsuits* is an indicator for fiscal years coinciding with the class period for any lawsuit (e.g. breach of any law, including security law, energy law, international law, employment law, etc.) with positive settlement amount. *Backdating* is an indicator for firm years for which firms are convicted of backdating or misdating. Governance reduction for a standard deviation change in ExecLawyer delta in the hiring year is presented at the bottom of the table. It is then compared to the pre-hiring mean of the governance failure measure (Appendix Table 3) to calculate reduction percentage. Reduction as a percentage of governance improvement is the ratio of governance reduction to governance improvement (Table 3). Standard errors are clustered at the firm level. Superscripts ***, **, * indicate statistical significance level at the 1%, 5%, and 10% level, respectively.

	(1) Securities Fraud	(2) Securities Fraud	(3) Securities Fraud	(4) General Lawsuits	(5) General Lawsuits	(6) General Lawsuits	(7) Back-dating	(8) Back-dating	(9) Back-dating
Post	0.021	0.183	0.188	0.053	0.209	0.193	-0.026	0.019	0.005
	[0.051]	[0.132]	[0.146]	[0.046]	[0.128]	[0.146]	[0.035]	[0.123]	[0.121]
CorporateHire	-0.027	0.021	0.022	-0.055	0.051	0.051	-0.049	0.11	0.106
	[0.024]	[0.087]	[0.087]	[0.036]	[0.160]	[0.159]	[0.033]	[0.129]	[0.131]
Post*CorporateHire	0.019	-0.253*	-0.268*	0.002	-0.275*	-0.242	0.004	-0.066	-0.033
	[0.039]	[0.138]	[0.148]	[0.044]	[0.154]	[0.170]	[0.013]	[0.105]	[0.117]
Log(ExecLawyerDelta)		-0.006	-0.006		0.033	0.032		0.037	0.035
		[0.019]	[0.018]		[0.049]	[0.047]		[0.032]	[0.032]
Post*Log(ExecLawyerDelta)		-0.052	-0.05		-0.05	-0.055		-0.016	-0.021
		[0.034]	[0.032]		[0.035]	[0.036]		[0.034]	[0.035]
CorporateHire*Log(ExecLawyerDelta)		-0.016	-0.016		-0.034	-0.033		-0.053	-0.052
		[0.023]	[0.023]		[0.048]	[0.048]		[0.045]	[0.045]
Post*CorporateHire*Log(ExecLawyerDelta)		**0.088****	**0.084****		**0.089****	**0.099****		**0.024**	**0.032**
		[0.038]	**[0.038]**		**[0.043]**	**[0.046]**		**[0.039]**	**[0.039]**
Post*Log(CEODelta)			-0.002			0.006			0.005
			[0.014]			[0.018]			[0.007]
Post*CorporateHire*Log(CEODelta)			0.005			-0.011			-0.01
			[0.018]			[0.026]			[0.010]
Hire Year F.E.	Y	Y	Y	Y	Y	Y	Y	Y	Y
Calendar Year F.E.	Y	Y	Y	Y	Y	Y	Y	Y	Y
SIC Two-Digit F.E.	Y	Y	Y	Y	Y	Y	Y	Y	Y
Observations	910	910	910	910	910	910	452	452	452
R-squared	0.179	0.192	0.193	0.170	0.177	0.177	0.284	0.295	0.296
Pre-Hire Mean		*0.047*	*0.047*		*0.085*	*0.085*			
Given a one standard deviation increase in Log(ExecLawyerDelta):									
Magnitude of governance improvement		*0.020*	*0.020*		*0.024*	*0.024*			
Governance reduction (in % points)		*0.017*	*0.016*		*0.017*	*0.019*			
Governance reduction (in % change) given		*36.3%*	*34.6%*		*20.2%*	*22.5%*			
Reduction as % of governance improvement		*87.5%*	*83.5%*		*71.9%*	*80.0%*			

Table 7: The Effect of ExecLawyer Equity Incentives on Monitoring - Collapsed Estimation

This table presents collapsed double and triple differencing estimations of the effect of ExecLawyer incentive pay on monitoring failures, 1995-2012. The treatment group is corporations hiring ExecLawyers from other corporations, and the control group is firms that hire ExecLawyers from law firms, matched within the year-industry-size and by the propensity score of hiring from law firms vs. corporations. The dependent variable is the change of monitoring failure measure from pre- to post-hiring period. CEO delta and ExecLawyer delta are the respective manager's total wealth to performance sensitivities based on stock holdings and unexercised options in constant 2012 (million) dollars, following Core and Guay (1999). *Securities Fraud* is an indicator that takes on the value of one for fiscal years coinciding with the class period identified by the securities class action lawsuits. *General Lawsuits* is an indicator for fiscal years coinciding with the class period for any lawsuit (e.g. breach of any law, including security law, energy law, international law, employment law, etc.) with positive settlement amount. *Backdating* is an indicator for firm years for which firms are convicted of backdating or misdating. Governance reduction for a standard deviation change in ExecLawyer delta in the hiring year is presented at the bottom of the table. It is then compared to the pre-hiring mean of the governance failure measure (Appendix Table 3) to calculate reduction percentage. Reduction as a percentage of governance improvement is the ratio of governance reduction to governance improvement (Table 3). Standard errors are clustered at the firm level. Superscripts ***, **, * indicate statistical significance level at the 1%, 5%, and 10% level, respectively.

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
	Securities Fraud	Securities Fraud	Securities Fraud	General Lawsuits	General Lawsuits	General Lawsuits	Back-dating	Back-dating	Back-dating
CorporateHire	-0.01	-0.223*	-0.129	-0.007	-0.217*	-0.215	0.013	-0.158	-0.171
	[0.037]	[0.118]	[0.157]	[0.037]	[0.131]	[0.167]	[0.018]	[0.150]	[0.157]
Log(ExecLawyerDelta)		-0.019	-0.033		-0.018	-0.024		-0.049	-0.046
		[0.023]	[0.026]		[0.029]	[0.028]		[0.054]	[0.053]
CorporateHire*Log(ExecLawyerDelta)		**0.078****	**0.087****		**0.076***	**0.076***		**0.066**	**0.068**
		[0.036]	**[0.038]**		**[0.041]**	**[0.042]**		**[0.059]**	**[0.060]**
Log(CEODelta)			0.025			0.010			-0.013
			[0.021]			[0.016]			[0.013]
CorporateHire*Log(CEODelta)			-0.021			0.000			0.002
			[0.026]			[0.023]			[0.017]
Hire Year F.E.	Y	Y	Y	Y	Y	Y	Y	Y	Y
SIC One-Digit F.E.	Y	Y	Y	Y	Y	Y	Y	Y	Y
Observations	413	413	413	413	413	413	269	269	269
R-squared	0.070	0.076	0.082	0.095	0.101	0.102	0.108	0.134	0.151
Pre-Hire Mean		*0.047*	*0.047*		*0.085*	*0.085*			
Given a one standard deviation increase in Log(ExecLawyerDelta):									
Magnitude of governance improvement		*0.020*	*0.020*		*0.024*	*0.024*			
Governance reduction (in % points)		*0.016*	*0.018*		*0.015*	*0.015*			
Governance reduction (in % change) given		*33.6%*	*37.4%*		*18.0%*	*18.0%*			
Reduction as % of governance improvement		*81.0%*	*90.3%*		*64.1%*	*64.1%*			

Table 8: The Effect of ExecLawyer Equity Incentives on Business Development

This table presents double and triple differencing estimations of the effect of ExecLawyer incentive pay on business development, 1995-2012. Columns (3), (6) and (9) remove observations with zero ExecLawyerDelta. The treatment group is corporations hiring ExecLawyers from other corporations, and the control group is firms that hire ExecLawyers from law firms, matched within the year-industry-size and by the propensity score of hiring from law firms vs. corporations. Post is set to zero for the two years prior to the hiring of ExecLawyer, and one for the two years subsequent. The year of hiring is tossed out. CEO delta and ExecLawyer delta are the respective manager's total wealth to performance sensitivities based on stock holdings and unexercised options in constant 2012 (million) dollars, following Core and Guay (1999). *CapEx* is the ratio of capital expediture to PP&E measured at the beginning of the fiscal year. *R&D* is the R&D expenses scaled by assets at the beginning of the fiscal year. *Business segments* are in counts of business lines, capturing complexity. Governance reduction for a standard deviation change in ExecLawyer delta in the hiring year is presented at the bottom of the table. It is then compared to the pre-hiring mean of the governance failure measure (Appendix Table 3) to calculate reduction percentage. Reduction as a percentage of governance improvement is the ratio of governance reduction to governance improvement (Table 3). Standard errors are clustered at the firm level. Superscripts ***, **, * indicate statistical significance level at the 1%, 5%, and 10% level, respectively.

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Sample only non-zero deltas?	No	No	Yes	No	No	Yes	No	No	Yes
Dependent variable:	Capex	Capex	Capex	R&D	R&D	R&D	Business segments	Business segments	Business segments
Post	0.06	0.128	0.122	0.023*	0.037	0.084*	0.454*	0.241	0.775
	[0.072]	[0.131]	[0.186]	[0.013]	[0.030]	[0.051]	[0.247]	[0.889]	[1.037]
CorporateHire	0.017	0.062	0.100	-0.003	-0.033	-0.058	-0.415	0.310	-2.762
	[0.040]	[0.142]	[0.226]	[0.011]	[0.044]	[0.051]	[0.444]	[2.208]	[2.897]
Post*CorporateHire	-0.038	-0.238	-0.348*	-0.008	-0.016	-0.076	-0.433	1.256	0.746
	[0.043]	[0.145]	[0.189]	[0.010]	[0.036]	[0.060]	[0.289]	[1.551]	[2.039]
Log(ExecLawyerDelta)		0.010	0.048		-0.004	0.007		0.271	0.106
		[0.040]	[0.047]		[0.008]	[0.007]		[0.460]	[0.638]
Post*Log(ExecLawyerDelta)		-0.028	-0.043		-0.001	0.018***		-0.155	-0.119
		[0.042]	[0.051]		[0.005]	[0.006]		[0.255]	[0.302]
CorporateHire*Log(ExecLawyerDelta)		-0.016	-0.024		0.011	0.018		-0.255	0.637
		[0.046]	[0.065]		[0.014]	[0.016]		[0.815]	[0.935]
Post*CorporateHire*Log(ExecLawyerDelta)		**0.089***	**0.083**		**0.006**	**0.024****		**0.303**	**0.188**
		[0.052]	**[0.067]**		**[0.008]**	**[0.010]**		**[0.418]**	**[0.498]**
Post*Log(CEODelta)		0.002	-0.008		-0.002	0.000		0.102	0.02
		[0.009]	[0.011]		[0.004]	[0.005]		[0.189]	[0.212]
Post*CorporateHire*Log(CEODelta)		-0.008	0.012		-0.002	-0.003		-0.461	-0.303
		[0.016]	[0.022]		[0.005]	[0.006]		[0.318]	[0.318]
Hire Year F.E.	Y	Y	Y	Y	Y	Y	Y	Y	Y
Calendar Year F.E.	Y	Y	Y	Y	Y	Y	Y	Y	Y
SIC Two-Digit F.E.	Y	Y	Y	Y	Y	Y	Y	Y	Y
Observations	1,642	1,642	910	1,658	1,658	906	1,650	1,650	910
R-squared	0.161	0.163	0.183	0.253	0.255	0.292	0.335	0.339	0.441
Pre-Hire Mean		*0.314*				*0.047*			
Given a one standard deviation increase in Log(ExecLawyerDelta):									
Magnitude of governance improvement		*0.017*				*0.005*			
Governance reduction (in % points)		*0.053*				*0.100*			

Appendix Table 1: Variable Definition, Data Sources and Descriptive Statistics

This table presents the definition and sources of the variables used in the study and shows the summary statistics of the variables.

Variable name	Variable definition	Sources	N	Mean	Median	Std
ExecLawyer Background						
ExecLawyer	Indicator variable that takes on the value of one if a general counsel appears in ExecuComp as one of the top paid executives.	Execucomp	32,372	0.393	0	0.488
ExecLawyer age	The age of the ExecLawyer	Execucomp, Def 14As and 10-Ks	12,562	50.891	51	7.281
(The statistics below are based on unique ExecLawyer-Firm observations where the immediate job experience prior to ExecLawyer is available)						
Internal	ExecLawyer was internally promoted	Execucomp, Def 14As and 10-Ks	2,600	0.274	0.000	0.446
Law Firm Hire	Indicator variable that takes on the value of one if an ExecGC was hired directly from a law firm.	Def 14As, 10-Ks, Matindale-Hubbard, LinkedIn, online searches	2,600	0.272	0.000	0.445
Corporate Hire	Indicator variable that takes on the value of one if an ExecGC was hired directly from another corporation	Def 14As, 10-Ks, Matindale-Hubbard, LinkedIn, online searches	2,600	0.444	0.000	0.497
Government Officials	Indicator variable that takes on the value of one if an ExecLawyer held important government positions (e.g. Attorney General, White House Counsel, Judge, Federal Attorney, Department of Justice etc.) before becoming a GC.	Def 14As, 10-Ks, Matindale-Hubbard, LinkedIn, online searches	2,600	0.007	0.000	0.081
Compensation						
ExecLawyer pay	ExecLawyer total compensation (salary, bonus, other cash compensation, option grants, and restricted stocks) in constant 2012 dollars.	Execucomp	12,709	1,445	800	3,678
CEO pay	CEO total compensation (salary, bonus, other cash compensation, option grants, and restricted stocks) in constant 2012 dollars.	Execucomp	12,207	6,580	3,002	26,400
ExecLawyer pay / CEO pay	Total compensation of the ExecGC to the total compensation of the CEO.	Execucomp	12,177	0.378	0.301	0.378
ExecLawyer delta	Total wealth for performance sensitivities based on stock holdings and unexercised options in constant 2012 (million) dollars based on Core and Guay (1999).	Execucomp	12,361	0.055	0.020	0.201
CEO delta	Total wealth for performance sensitivities based on stock holdings and unexercised options in constant 2012 (million) dollars based on Core and Guay (1999).	Execucomp	11,793	0.865	0.201	4.501
Compliance Failures						
AAER Fraud	Indicator that takes on the value of one if the financial statements of a given fiscal year are restated and investigated by the SEC. Accounting and Auditing Enforcement Releases are issued by the SEC during or at the conclusion of an investigation against a company, an auditor, or an officer for alleged accounting and/or auditing misconduct. This variable is set equal to missing for fiscal years after 2009.	Center for Financial Reporting and Management Center at the Haas School of Business	27,444	0.020	0.000	0.140
SEC Insider Trading	Indicator that is one if in a given year a corporate executive traded his/her own company's stock based on insider information or tipped such information for others to trade and later was investigated by the SEC, and zero otherwise.	SEC Litigation Releases on Enforcement Actions on Insider Trading	32,372	0.004	0.000	0.067

Variable name	Variable definition	Sources	N	Mean	Median	Std
Monitoring Failures						
Securities Fraud	Indicator that takes on the value of one for fiscal years coinciding the class period identified by the securities class action lawsuits. Dismissed cases are dropped for defining this variable.	Stanford Law School Securities Class Action Clearing House	32,372	0.029	0.000	0.169
General Lawsuits	Indicator that takes on the value of one for fiscal years coinciding the class period identified by the securities class action lawsuits or other lawsuits (e.g. breach of any law, including security law, energy law, international law, employment law, etc.) with positive settlement amount.	Audit Analytics	32,372	0.056	0.000	0.231
Backdating	Indicator that takes on the value of one for firm years for which firms are convicted of backdating or misdating.	Wall Street Journal	23,899	0.014	0.000	0.117
Business Development						
Capex	The ratio of capital expediture to PP&E at the beginning of the fiscal year	Compustat	31,064	0.305	0.202	0.418
R&D	R&D expenses scaled by assets at the beginning of the fiscal year	Compustat	32,275	0.055	0.014	0.156
Business segments	Number of business segments	Compustat segments	32,372	5.041	3.000	4.567
Firm Characteristics						
Assets	Book value of assets in millions of constant 2012 dollars.	Compustat	32,372	15,962	1,951	91,367
Sales	Sales in millions of constant 2012 dollars.	Compustat	32,359	6,010	1,419	18,301
Marketcap	Market capitalization in millions of constant 2012 dollars.	Compustat	32,127	8,156	1,683	26,757
Market-adjusted returns	Annual cumulative stock returns minus cumulative market (CRSP value weighted) returns over the fiscal year.	CRSP	31,712	0.080	-0.006	0.682
Market to Book	The ratio of market value of asset (market value of equity, plus book value of debt and book value of preferred equity, minus deferred taxes) to book value of assets.	Compustat	31,880	1.631	1.139	2.094
Leverage	The ratio of total liabilities to book assets	Compustat	32,284	0.566	0.560	0.287
ROA	The ratio of EBITDA to book assets	Compustat	31,527	0.120	0.123	0.143
Firm age	Number of years since a firm first appears on CRSP (use the median of the sample if missing).	CRSP	31,726	22.687	17.178	18.627
Other Governance Measures						
Board independence	Percentage of independent directors on board	Riskmetrics	25,023	69.292	71.429	16.914
Governance Index	Gompers, Ishii and Metrick (2003) governance index	Riskmetrics	17,512	9.225	9.000	2.644

Appendix Table 2: CEO Fixed Effects on Compliance, Monitoring and Business Development Using CEO Movers

This table presents CEO fixed effects, 1995-2012. Each row represents a regression for the dependent variable to the left. The sample is limited to firm-year observations for CEOs that move. The fixed effects included are: year and firm fixed effects in row 1; year, firm, and CEO fixed effects in row 2. Reported in the second column are F-tests for the joint significance of the CEO fixed effects. For each F-test, we report the value of the F-statistic, the p-value, and the number of constraints. The final two columns report the adjusted R-squared and the partial adjusted r-square for CEOs. *AAER Fraud* is an indicator for a restatement investigation by the SEC covering the observation year. *SEC Insider Trading* is an indicator for an executive being investigated for insider trading by the SEC. *Securities Fraud* is an indicator that takes on the value of one for fiscal years coinciding with the class period identified by the securities class action lawsuits. *General Lawsuits* is an indicator for fiscal years coinciding with the class period for any lawsuit (e.g. breach of any law, including security law, energy law, international law, employment law, etc.) with positive settlement amount. *Backdating* is an indicator for firm years for which firms are convicted of backdating or misdating. *CapEx* is the ratio of capital expediture to PP&E measured at the beginning of the fiscal year. *R&D* is the R&D expenses scaled by assets at the beginning of the fiscal year. *Business segments* are in counts of business lines, capturing complexity.

	F-tests on fixed effects for CEOs	N	Adjusted R-squared	CEO Partial R-squared
Compliance Failures				
AAER Fraud		2,344	0.339	
	3.75*** (<.0001, 275)	2,344	0.584	0.245
SEC Insider Trading		2,719	0.016	
	1.87*** (<.0001, 327)	2,719	0.163	0.147
Monitoring Failures				
Securities Fraud		2,719	0.193	
	2.55*** (<.0001, 327)	2,719	0.386	0.193
General Lawsuits		2,719	0.434	
	2.09*** (<.0001, 327)	2,719	0.536	0.102
Backdating		2,204	0.160	
	6.31*** (<.0001, 265)	2,204	0.640	0.480
Business Development				
Capex		2,579	0.478	
	1.71*** (<.0001, 318)	2,579	0.546	0.068
R&D		2,703	0.319	
	0.801 (.9918, 327)	2,703	0.291	-
Business segments		2,719	0.775	
	2.30*** (<.0001, 327)	2,719	0.822	0.047

Appendix Table 3: Summary Statistics with ExecLawyer Hiring Firms vs. No-ExecLawyer Firms

Executive lawyer (ExecLawyer) refers to a general counsel that appears in ExecuComp as one of the top paid executives and stays in position for three consecutive years. This table presents firm and manager statistics taken in the year when the ExecLawyer is hired. Firms with no ExecLawyer include firm years where there is no ExecLawyer in a five-year window (i.e., from two years prior to two years after). ExecLawyer pay is the executive lawyer's total compensation (salary, bonus, other cash compensation, option grants, and restricted stocks) in constant 2012 dollars. CEO pay is the CEO's total compensation. CEO delta and ExecLawyer delta are the respective manager's total wealth to performance sensitivities based on stock holdings and unexercised options in constant 2012 (million) dollars, following Core and Guay (1999). AAER Fraud is an indicator for a restatement investigation by the SEC covering the observation year. SEC Insider Trading is an indicator for an executive being investigated for insider trading by the SEC. Securities Fraud is an indicator that takes on the value of one for fiscal years coinciding with the class period identified by the securities class action lawsuits. General Lawsuits is an indicator for fiscal years coinciding with the class period for any lawsuit (e.g. breach of any law, including security law, energy law, international law, employment law, etc.) with positive settlement amount. Backdating is an indicator for firm years for which firms are convicted of backdating or misdating. CapEx is the ratio of capital expediture to PP&E measured at the beginning of the fiscal year. R&D is the R&D expenses scaled by assets at the beginning of the fiscal year. Business segments are in counts of business lines, capturing complexity.Assets, Sales, and Market Capitalization (Marketcap) are from the balance sheet in millions of constant 2012 dollars. Market-adjusted returns are annual cumulative stock returns minus cumulative market (CRSP value weighted) returns over the fiscal year. Market to Book is the ratio of market value of asset (market value of equity, plus book value of debt and book value of preferred equity, minus deferred taxes) to book value of assets. Leverage is the ratio of total liabilities to book assets. ROA is EBITDA scaled by book assets. Firm age is the number of years since a firm first appears on CRSP. Board independence is the percentage of independent directors on board. Governance index is the Gompers, Ishii and Metrick (2003) governance index. Our sample comprises firm years in ExecuComp 1995-2012.

	ExecLawyer Hiring Year		No ExecLawyer		Difference
# of Obs.	574		9,004		
	Mean	Std	Mean	Std	p-value
Compensation					
ExecLawyer Pay ($ thousand)	1,036	2,032	.	.	
CEO Pay ($ thousand)	6,043	10,800	7,032	28,663	0.413
ExecLawyer pay / CEO pay	0.318	0.438	.	.	
ExecLawyer delta ($ million)	0.016	0.053	.	.	
CEO delta ($ million)	0.998	4.121	3.541	61.052	0.328
Compliance Failures					
AAER Fraud	0.035	0.183	0.022	0.145	0.051
SEC Insider Trading	0.005	0.072	0.005	0.069	0.880
Monitoring Failures					
Securities Fraud	0.047	0.212	0.028	0.166	0.010
General Lawsuits	0.085	0.280	0.053	0.224	0.001
Backdating	0.018	0.133	0.023	0.150	0.496
Business Development					
Capex	0.314	0.390	0.299	0.363	0.330
R&D	0.047	0.114	0.063	0.187	0.036
Business segments	5.970	4.967	5.329	4.593	0.001
Firm Characteristics					
Assets	16,775	78,826	19,829	111,110	0.517
Sales	6,009	16,340	6,509	20,760	0.572
Marketcap	7,431	21,085	9,834	31,465	0.071
Market-adjusted returns	0.066	0.641	0.114	0.772	0.146
Market to Book	1.596	1.556	1.766	2.107	0.059
Leverage	0.564	0.268	0.522	0.245	0.000
ROA	0.118	0.169	0.128	0.122	0.064
Firm age	21.877	17.394	21.706	16.657	0.812
Other Governance Measures					
Board independence	68.970	16.461	66.605	16.868	0.003
Governance index	9.271	2.514	8.792	2.639	0.001

Appendix Table 4: Logit Regression on ExecLawyer Hiring

This table presents the logit regression on ExecLawyer hiring. The dependent variable in column (1) takes on the value one of a firm hires an ExecLawyer but has no ExecLawyer in any of the two prior years, and zero if a firm has no ExecLawyer in the current year as well as any of the prior to years. The dependent variable in column (2) takes on the value of one if a firm hires an ExecLawyer from a law firm, and zero if a firm poaches an ExecLawyer from another corporation. Our sample comprises firm years in ExecuComp from 1995 to 2012. Detailed variable definitions are provided in Appendix Table 1. Standard errors are clustered at the firm level. Superscripts ***, **, * indicate statistical significance level at the 1%, 5%, and 10% level, respectively.

	(1) Dependent = 1 if Hiring ExecLawyer	(2) Dependent = 1 if Hiring ExecLawyer from Law Firm
AAER Fraud	0.705***	0.128
	(0.237)	(0.484)
SEC Insider Trading	0.207	0.544
	(0.754)	(1.509)
Class action litigation	0.272	0.674
	(0.239)	(0.484)
Log(marketcap)	0.021	-0.054
	(0.032)	(0.072)
Market-adjusted returns	-0.050	0.291*
	(0.069)	(0.160)
Market to Book	-0.024	-0.049
	(0.031)	(0.072)
Leverage	0.986***	-0.479
	(0.218)	(0.472)
ROA	-0.444	0.043
	(0.392)	(0.970)
Firm age	-0.005*	-0.005
	(0.003)	(0.006)
Capex	0.023**	-0.008
	(0.010)	(0.022)
R&D	-0.782*	-0.289
	(0.448)	(0.757)
Business segments	0.246**	-0.276
	(0.100)	(0.231)
Trend	-0.257***	0.159
	(0.067)	(0.146)
Trend^2	0.012***	-0.009
	(0.003)	(0.007)
SIC One-Digit F.E.	Y	Y
Observations	9,034	536
Pesudo R-squared	0.025	0.043

Appendix Table 5: Summary Statistics with ExecLawyers Hired from Corporations vs. ExecLawyers Hired from Law Firms

This table presents statistics taken in the year when the ExecLawyer is hired, by the two different career sources from which ExecLawyers are hired. The treatment group is corporations hiring ExecLawyers from other corporations, and the control group is firms that are matched within the year-industry-size and by propensity score and hire ExecLawyers from law firms. Manager pay is the executive's total compensation (salary, bonus, other cash compensation, option grants, and restricted stocks) in constant 2012 dollars. CEO delta and ExecLawyer delta are the respective manager's total wealth to performance sensitivities based on stock holdings and unexercised options in constant 2012 (million) dollars, following Core and Guay (1999). ExecLawyer age is the age of the ExecLawyer. AAER Fraud is an indicator for a restatement investigation by the SEC covering the observation year. SEC Insider Trading is an indicator for an executive being investigated for insider trading by the SEC. Securities Fraud is an indicator that takes on the value of one for fiscal years coinciding with the class period identified by the securities class action lawsuits. General Lawsuits is an indicator for fiscal years coinciding with the class period for any lawsuit (e.g. breach of any law, including security law, energy law, international law, employment law, etc.) with positive settlement amount. Backdating is an indicator for firm years for which firms are convicted of backdating or misdating. CapEx is the ratio of capital expediture to PP&E measured at the beginning of the fiscal year. R&D is the R&D expenses scaled by assets at the beginning of the fiscal year. Business segments are in counts of business lines, capturing complexity. Assets, Sales, and Market Capitalization (Marketcap) are from the balance sheet in millions of constant 2012 dollars. Market-adjusted returns are cumulative stock returns minus cumulative market (CRSP value weighted) returns over the fiscal year. Market to Book is the ratio of market value of asset (market value of equity, plus book value of debt and book value of preferred equity, minus deferred taxes) to book value of assets. Leverage is the ratio of total liabilities to book assets. ROA is the ratio of EBITDA to book assets. Firm age is the number of years since a firm first appears on CRSP. Board independence is the percentage of independent directors on board. Governance index is the Gompers, Ishii and Metrick (2003) governance index.

	Corporate Hire		Law Firm Hire		Difference
Obs. (unmatched)	361		213		
Obs. (matched)	227		189		
	Mean	Std	Mean	Std	p-value
Compensation					
ExecLawyer Pay ($ thousand)	889	2,205	1,042	1,982	0.363
CEO Pay ($ thousand)	5,963	9,827	6,029	10,767	0.954
ExecLawyer pay / CEO pay	0.265	0.318	0.327	0.432	0.119
ExecLawyer delta ($ million)	0.010	0.025	0.015	0.049	0.214
CEO delta ($ million)	1.361	2.973	0.975	0.027	0.631
ExecLawyer age	49.4	6.7	48.7	2.6	0.394
Compliance Failures					
AAER Fraud	0.042	0.181	0.028	0.166	0.510
SEC Insider Trading	0.000	0.000	0.005	0.073	0.318
Monitoring Failures					
Securities Fraud	0.051	0.185	0.069	0.254	0.567
General Lawsuits	0.086	0.271	0.106	0.308	0.586
Backdating	0.014	0.128	0.031	0.175	0.300
Business Development					
Capex	0.347	0.470	0.313	0.351	0.547
R&D	0.041	0.056	0.055	0.171	0.298
Business segments	5.599	5.089	5.952	4.948	0.519
Firm Characteristics					
Assets	10,905	16,700	13,151	48,147	0.612
Sales	5,305	10,241	7,258	23,867	0.313
Marketcap	7,096	22,089	7,777	21,832	0.751
Market-adjusted returns	0.074	0.685	0.082	0.622	0.925
Market to Book	1.494	1.481	1.734	1.857	0.160
Leverage	0.577	0.244	0.549	0.222	0.312
ROA	0.115	0.126	0.116	0.224	0.943
Firm age	24.0	16.8	21.4	17.3	0.202
Other Governance Measures					
Board independence	70.224	16.963	67.176	14.733	0.132
Governance index	9.473	2.444	9.100	2.588	0.237