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Top Managers' Political Conservatism and External Governance Choices*

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Abstract

We develop a theory of *corporate governance conservatism* that reflects the preference of politically conservative chief executive officers (CEOs) for stability and continuity in corporate governance provisions without managerial entrenchment. Our theory suggests that conservative CEOs tend to prefer corporate governance provisions against hostile takeover and drastic board turnover, but their emphasis on hard work and self-discipline are likely to lead them to run their firms more efficiently with less debt. Using a sample of 2,339 U.S. corporations in the 1996-2006 period, we find strong empirical support for this new theory. Firms with Republican CEOs, who are known to be politically conservative, are more likely to stagger the terms and elections of directors, limit shareholders' ability to amend corporate bylaws and require supermajority for approval of mergers, but those CEOs are not associated with a significant impairment in shareholders' value. Rather, we find firms run by Republican CEOs tend to have higher return on assets and lower leverage, consistent with the results documented by Hutton, Jiang, and Kumar (2014). Overall, our theory and empirical results highlight an important spillover effect of top managers'

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political conservatism on corporate governance choices. We further discuss other dimensions of corporate governance that could also reflect top managers' political conservatism.

Key words: CEO political conservatism, corporate governance conservatism, external governance choices, entrenchment discount, *G Index*, *E Index*, staggered board, limits to amend bylaws, supermajority
JEL Classification: G34

INTRODUCTION

Conservatism is a disposition in politics to maintain the existing order (Morris, 1976). Political conservatives support retaining traditional institutions and are opposed to disruptive changes in the social, economic, and legal order. Also, they have greater need for cognitive closure, therefore, prefer unambiguous and non-probabilistic outcomes (Jost, Glaser, Kruglanski, and Sulloway, 2003a). If these tendencies of political conservatives could be reflected in corporate decision making through conservative attitudes of top managers, what would be implications of the political conservatism for corporate governance choices? Are firms run by politically conservative managers more likely to have governance provisions shielding them from external influences such as hostile takeover and drastic board turnover? More importantly, does this lack of external disciplining mechanisms result in managerial entrenchment? The latter question is important to answer in order to conclude whether the seemingly-poor governance mechanisms found in firms with politically conservative managers are simply a reflection of the managers' conservative attitudes or they actually lead to managerial entrenchment. In this paper, we test these important corporate governance questions.

In the U.S., conservatism has been primarily associated with the Republican Party. Conservatism has served the ideological core of the Republican Party, contrasting with the liberalism of the Democrats. Core tenets of conservatism have been reflected in the Republican Party's platforms.[1)] Also, survey results indicate that

1) Core values of American conservatism such as free enterprise, minimum taxes and government regulations, traditional family and marriage, and religious freedom can be found in the Republican Party's platforms. See https://www.gop.com/platform/.

over two thirds of Republicans consider themselves conservative.[2] Therefore, for our empirical analysis, we define top managers who support the Republican Party via individual political contributions to be politically conservative.

We start out our analysis by developing a theory of *corporate governance conservatism*. Based on the key arguments made in political psychology literature (Jost, Glaser, Kruglanski, and Sulloway, 2003a, 2003b), which emphasize two core psychological traits of political conservatives – resistance to external changes and aversion to ambiguous outcomes and equality, we develop a notion of corporate governance conservatism such that Republican CEOs, who are politically conservative, prefer corporate governance provisions which protect them from external interventions and radical changes in board composition. However, this notion of governance conservatism does not necessarily imply managerial entrenchment problems due in part to the strong internal governance of Republican CEOs who emphasize hard work and frugality (Furnham, 1982; Furnham and Bland, 1983).

We then test our theory of *corporate governance conservatism* for the CEOs of 2,339 publicly traded companies in the U.S. that are at the intersection of the ExecuComp and Institutional Shareholder Services (ISS) databases over the period of 1996 to 2006.[3] We identify the political orientation of the CEOs using their political donation history. In particular, we track each CEO's full history of individual political donations since 1989, measure the relative tilt of the CEO's donations toward the Republican Party by comparing the dollar amounts of donations made to the Republican vs. Democratic Parties, and denote it by *CEO Rep Index* (Hong and Kostovetsky, 2012; Hutton, Jiang, and Kumar, 2014; Lee, Lee, and Nagarajan, 2014).

We find that firms with Republican CEOs are more likely to have governance provisions that shield their managers from external disciplining mechanisms. For a one standard deviation increase in *CEO Rep Index*, there is 2.20% increase in *G Index* (Gompers, Ishii, and Metrick, 2003) from its sample average. We find a similar economic impact on *E Index* (Bebchuk, Cohen, and

2) See http://www.gallup.com/poll/180452/liberals-record-trail-conservatives.aspx.

3) ISS database was formerly named Investor Responsibility Research Center (or RiskMetrics) database.

Ferrell, 2009), which corresponds to a 3.73% increase from its sample average. These economically meaningful effects of CEO's political conservatism on governance provisions are also statistically significant at the 1% level.

Additional tests show that these results are not driven by politically inactive CEOs who made no donations at all or independent directors who also support the Republican Party. Further, we find our results hold when we define political orientation only for political polarizers who donate to only one party, either Republican or Democratic, but not both. Finally, we find that it is Republican CEOs rather than Democratic CEOs who drive our main empirical results.

We continue to conduct our analysis at each governance provision level and further find that staggered boards, limits to amend bylaws, and supermajority provisions are the ones that are most likely to be associated with Republican CEOs among the six governance provisions that constitute *E Index*. The results are in line with the main prediction of our theory that conservative CEOs prefer stability and continuity in organizational structure and seek to avoid ambiguous voting outcomes. For other provisions that are specifically related to their personal compensation, we do not find evidence indicating that Republican CEOs are more likely to be protected by provisions such as *Golden Parachute*, *Compensation Plan*, and *Severance* provisions. These results could be interpreted as a revelation of the Republican CEOs' strong work ethic emphasizing hard work.

As robustness checks, we show that any omitted CEO personal characteristics such as age, gender, tenure, board chairmanship, and company stock holdings do not drive our main empirical results. In addition, we sharpen the notion of corporate governance conservatism by showing that Republican CEOs do not lead to significant managerial entrenchment problems in spite of the seemingly-poor governance provisions found in their firms. Consistent with the financial conservatism of Republican CEOs documented by Hutton, Jiang, and Kumar (2014), we find that firms with Republican CEOs tend to have higher profitability but lower leverage.

Overall our findings show an important spillover effect of the CEO political conservatism on external corporate governance choices. In our final discussion, we further extend this notion of corporate

governance conservatism to other governance topics by developing a theory that shows how top managers' political conservatism could affect board diversity – an important dimension that has received growing attention in recent years in the corporate governance literature.

We make a number of contributions in this paper. We are the first to develop the notion of corporate governance conservatism for firms run by Republican CEOs. Several studies document different preferences and personal values between Republican and Democratic managers; corporate social responsibility of Democratic money managers and CEOs (Hong and Kostovetsky, 2012; DiGiuli and Kostovetsky, 2014), conservative corporate leverage policy by Republican managers (Hutton, Jiang, and Kumar, 2014), a firm's propensity to commit fraud as well as the types of fraud they commit (Hutton, Jiang, and Kumar, 2015). We extend these important discussions to firms' choice of governance provisions.

We also provide a theoretical discussion on the implication of corporate governance conservatism for boardroom diversity. In this regard, our study contributes to the burgeoning literature on boardroom diversity (Adams and Ferreira, 2004, 2009; Rhode and Packel, 2010; Masulis, Wang, and Xei, 2012; Lee, Lee, and Nagarajan, 2014).

We distinguish corporate governance conservatism from managerial entrenchment. During this discussion, we highlight different aspects of external governance choices, which are not necessarily linked to entrenchment motives. We, therefore, contribute to the managerial entrenchment and external governance literature that highlights the strong connection between corporate value and the mode of external governance (Gompers, Ishii, and Metrick, 2003; Bebchuk and Cohen, 2005; Bebchuk, Cohen, and Ferrell, 2009).

The remainder of this paper is organized as follows: Section 2 develops testable theories on corporate governance conservatism. Section 3 describes our data and introduces our main measure of the individual political conservatism – individual Republican Index. Section 4 presents our main empirical findings. In Section 5, we discuss other potential corporate governance choices that could also be affected by top managers' political conservatism. Section 6 concludes our study.

CORPORATE GOVERNANCE CONSERVATISM

In the U.S., conservatism has been chiefly associated with the Republican Party since the mid-20th century.[4] Core values of social and economic conservatives have been reflected in the Party's platforms,[5] and numerous poll results have indicated that the majority of Republicans identify themselves as conservatives.[6]

In an influential article, "Political conservatism as motivated social cognition," Jost, Glaser, Kruglanski, and Sulloway (2003a) propose two core dimensions of political conservatism – resistance to change and acceptance of inequality. Jost, Glaser, Kruglanski, and Sulloway (2003a, 2003b) further point out specific psychological motives and processes that are linked to the political conservatism including intolerance of ambiguity (Frenkel-Brunswik, 1949) and need for cognitive closure (Kruglanski and Webster, 1996), both of which are closely related to diversity aversion. Therefore, the literature suggests political conservatives support retaining traditional institutions and prefer stability and continuity. Their aversion to ambiguity and desire for cognitive closure could also imply their disinclination to probabilistic outcomes and diverse opinions.

What are the consequences of such political conservatism if it translates into conservative attitudes in corporate domains? The political ideology of individual top managers could influence various firm decisions including the choice of governance structure. In particular, Republican CEOs, who value stability and continuity, may prefer governance structure allowing them to run their firms over an extended period of time with less external intervention. If this is true, we conjecture that firms with Republican-leaning CEOs are more likely to have corporate governance provisions against

4) Although conservatism has much older roots in American history, its modern movement began to gel in the mid–1930s when intellectuals and politicians collaborated with businessmen to oppose the liberalism of the New Deal, led by President Franklin D. Roosevelt, newly energized labor unions, and big city Democratic machines. Before that, the Democratic Party had a conservative pro-business wing and also attracted strong support from catholic immigrants in the north as well as evangelical whites in the rural South. After President Roosevelt's New Deal, the business wing withered and, between the 1960s and the 1990s, Southern whites and many Catholics moved into the Republican Party. With the decline of the conservative wings of the Democratic Party, conservatism is most closely associated with the Republican Party.

5) See https://www.gop.com/platform/.

6) See http://www.gallup.com/poll/180452/liberals-record-trail-conservatives.aspx.

hostile takeover and drastic board turnover. They would also prefer stable, unambiguous, and deterministic outcomes of their decision making processes. All in all, one can hypothesize that firms run by Republican top managers are more likely to have governance provisions such as staggered board, limiting shareholders actions to change corporate bylaws and/or charters, and supermajority rules in their voting processes as a reflection of their conservative attitudes.

These corporate governance choices could result in significant firm value discount as suggested by existing studies that document that firms with governance provisions shielding managers from hostile takeover and/or preventing drastic board turnover suffer from entrenchment discounts (Gompers, Ishii, and Metrick, 2003; Bebchuk and Cohen, 2005; Bebchuk, Cohen, and Ferrell, 2009). Firms with Republican-leaning CEOs, therefore, could have a lower market value compared to those with non-Republican CEOs.

On the other hand, studies in psychology have shown that conservative beliefs are closely related to the Protestant work ethic which emphasizes hard work and frugality (e.g., Furnham, 1982; Furnham and Bland, 1983). Similarly, a recent survey on consumption and saving habits shows that conservatives tend to describe themselves as savers, save for retirement, and use financial investments as a way to save money.[7] Therefore, conservatives are more likely to support the personal responsibility that emphasizes individuals' hard work and disciplined spending and saving.

When such individual attributes of a Republican-leaning CEO is reflected in a firm's culture, it may have an impact on the firm's operating efficiency as well as its financial and investment policies. In particular, we conjecture that firms with a Republican-leaning CEO are more likely to have higher return on assets, make less risky investments and use debt more conservatively, which is consistent with the recent findings by Hutton, Jiang and Kumar (2014). Due in part to this economic conservatism, a Republican-leaning CEO may not be associated with significant firm value discount in spite of governance provisions that shield the manager from external disciplining mechanisms.

Such a mode of corporate governance, i.e., internally well-

7) See http://www.dailyfinance.com/2014/02/17/do-your-political-views-color-how-you-handle-money/.

disciplined Republican top managers choose seemingly-poor external governance provisions that could shield themselves from external changes and influences – is what we term "corporate governance conservatism." In what follows, we test for this corporate governance conservatism for firms run by Republican top managers in the U.S. private sectors.

DATA

Political donation data and Republican index

We consider the CEOs of 2,339 firms at the intersection of the ExecuComp and ISS databases over the period of 1996 to 2006. We use the annual CEO flag in the ExecuComp database to identify CEOs. To identify independent directors, we use the board affiliation in the ISS database. For each individual, we gather their political campaign donation records from the Federal Election Commission (FEC) following the matching algorithm used in Lee, Lee, and Nagarajan (2014).[8] Using this donation history, we measure the degree of each person's political orientation tilted toward the Republican Party by

$$Rep\ Index = \frac{R-D}{R+D}, \quad (1)$$

where R and D respectively denote the total dollar amounts of political donations made by an individual to the Republican and Democratic Parties over 11 federal election cycles since 1989. For a politically inactive individual, we assign zero to *Rep Index*. By construction, *Rep Index* ranges from -1 to 1, where a *Rep Index* of 1 (-1) indicates a "pure" republican (democrat) who has donated only to the Republican (Democratic) Party. Following Lee, Lee, and Nagarajan (2014), we use the full sample donation history to minimize any measurement errors. However, all our results are robust to using a *Rep Index* that is constructed using past donation records prior to the year of our interest. These results are available upon request.

For CEOs, we use their own *Rep Index*, whereas we use the average value of *Rep Index* for the group of independent directors.

8) See Section 2.1. of Lee, Lee, and Nagarajan (2014) for more details.

The former is denoted by *CEO Rep Index*, and we term the latter as *ID Rep Index*. Table 1 provides summary statistics for these two *Rep Index* variables. *CEO Rep Index* has a mean of 0.235, which implies that top managers of the U.S. corporations are more leaning toward the Republican Party. The mean value of *ID Rep Index* (0.097) indicates that independent directors on the boards are substantially less tilted toward the Republican Party than the CEOs. These donation patterns are consistent with the documentation by DiGiuli and Kostovetsky (2014) and Lee, Lee, and Nagarajan (2014).

Financial, corporate governance, and board characteristics

We construct financial variables using the financial data obtained from the Compustat and the Center for Research in Security Prices (CRSP) databases. We use the following financial variables: return on assets (*ROA*), Tobin's *Q*, investment intensity (*INV*), research and development intensity (*R&D*), market leverage ratio (*Mkt Lev*), cash flow volatility measured over the past five years (*CF Vol*), and the natural logarithm of inflation-adjusted book value of a firm's assets (*Log Assets*). Inflation is adjusted using the average consumer price index (CPI) from the U.S. Bureau of Labor Statistics (http://www.bls.gov/cpi/data.htm), whose value is normalized to be one for the year 1992. The formal definitions of these financial variables using the Compustat variable names are provided in Appendix. All these variables are winsorized at the 1% and 99% levels to minimize outlier effects.

Table 1 provides summary statistics for the financial variables. The average firm is profitable at 13.1% level (*ROA*), and its market value is around 1.927 times higher than its book value (*Q*). The average investment intensity is 21.5% of capital stocks. The average firm spends 2.6% of its book value of assets for research and development. On average, a firm has the inflation adjusted book assets of 1.68 billion (=$e^{7.426}$ million) in year 1992 dollars.

Next we summarize our governance variables. Information on firm-level external governance provisions and resulting *G Index* values are obtained from the ISS governance file. The *E Index* data are from Professor Lucian Bebchuk's web page.[9] The maximum *G Index* value is 24, and the index is available until year 2006. *E*

9) http://www.law.harvard.edu/faculty/bebchuk/data.shtml.

Table 1. Summary statistics

Political measures are explained in Section 3.1. Financial variables are explained in Section 3.2, and their formal definitions using Compustat variable names are provided in Appendix. Section 3.2 further explains corporate governance and board characteristics. *,**, and *** denote the statistical significance at the 10%-, 5%-, and 1%-level, respectively. The sample period is 1996-2006.

	N	Mean	Std.Dev.	Min	Median	Max
Political Measures						
CEO Rep Index	14,445	0.235	0.648	-1	0	1
ID Rep Index	14,658	0.097	0.283	-1	0.094	1
Financial Variables						
ROA	14,490	0.131	0.095	-0.298	0.127	0.426
Q	14,670	1.927	1.346	0.733	1.462	9.028
INV	14,691	0.215	0.159	0	0.184	0.862
R&D	14,691	0.026	0.050	0	0	0.297
Mkt Lev	14,628	0.167	0.152	0.000	0.135	0.968
CF Vol	13,899	0.038	0.040	0.001	0.026	0.258
Log Assets	14,683	7.426	1.640	3.342	7.230	11.841
Governance Measures						
G Index	13,263	9.259	2.657	1	9	19
E Index	11,870	2.467	1.300	0	3	6
Staggered Board	13,263	0.606	0.489	0	1	1
Limits to Amend Bylaws	13,263	0.193	0.395	0	0	1
Limits to Amend Charters	13,263	0.025	0.157	0	0	1
Supermajority	13,263	0.168	0.374	0	0	1
Golden Parachute	13,263	0.651	0.477	0	1	1
Poison Pill	13,263	0.576	0.494	0	1	1
Board Characteristics						
CEO Chairman (dummy)	14,445	0.941	0.235	0	1	1

	N	Mean	Std.Dev.	Min	Median	Max
CEO Age	13,688	55.858	7.440	32	56	91
CEO Tenure (year)	13,571	7.256	7.303	0	5	55
Female CEO (dummy)	14,445	0.013	0.112	0	0	1
CEO Stock Holding (%)	13,647	2.357	5.587	0	0	34.049
Board Size	14,691	9.605	2.934	3	9	39
Majority Independent	14,691	0.841	0.366	0	1	1
ID Group Age	14,658	60.320	4.640	35	60	83

Index has a maximum value of six and is available until year 2008. As these indices are not updated every year, we map the most up-to-dated values of these indices to each fiscal year end date for the firms in our sample.

As explained by Gompers, Ishii, and Metrick (2003), there are 24 provisions in *G Index* that are grouped into five different categories – Delay, Voting, Protection, Other, and State. Among them, the following six provisions constitute *E Index* (Bebchuk, Cohen, and Ferrell, 2009): *Staggered Board* provision from the Delay category, *Golden Parachute* from the Protection category, *Limits to Amend Bylaws*, *Limits to Amend Charters*, *Supermajority* from the Voting category, and finally *Poison Pill* from the Other category.

Staggered Board is a board in which directors are divided into separate classes, and each class is elected to overlapping terms. *Limits to Amend Bylaws* is a provision limiting shareholders' ability through majority vote to amend the corporate bylaws, and *Limits to Amend Charters* is a provision that limits shareholders' ability through majority vote to amend the corporate charters. *Supermajority* is a requirement for more than a majority of shareholders when approving a merger deal. *Golden Parachute* is a severance agreement that provides benefits to management and board members in the event of firing, demotion, or resignation following a change in control. Lastly, *Poison Pill* is a shareholder right that is triggered in the event of an unauthorized change in

control, which typically renders the target company financially unattractive or dilutes the voting power of the acquirer.

Table 1 shows the summary statistics of these corporate governance variables. The average values of *G* and *E Index* are 9.259 and 2.467, respectively. Looking further into each governance provision that constitutes the two external governance indices, we find that 60.6% of our sample firms have *Staggered Board* provision. As explained above, this provision protects incumbent directors from removal, resulting in a slow-moving board composition over time. Three provisions from the Voting category, *Limits to Amend Bylaws*, *Limits to Amend Charters*, and *Supermajority*, have the mean values of 19.3%, 2.5%, and 16.8%, respectively. Around 65.1% of our sample adopts *Golden Parachute*, while 57.6% adopts *Poison Pill*.

Lastly, we summarize the CEO and board members' characteristics in the same table. Data are obtained from ExecuComp and ISS director databases. Average CEOs tend to also hold the board chairman positions (0.941) and are 56 years old. They work in their office for about 7 years. Only 1.3% of our sample has a woman CEO. On average, CEOs hold 2.357% of company stocks. Average board consists of 9 to 10 members. The majority of them are independent directors for 84.1% of our sample. On average, independent directors are 60 years old, slightly older than the average CEOs.

We present the correlations between our main explanatory variable *CEO Rep Index* and our main dependent variable, *G Index*/ *E Index* and their constituent governance provisions in Table 2. First, we observe significantly high correlation (8.7% and 7.35%) between *CEO Rep Index* and both, *G-* and *E Index*, at the 1% statistical significance level. *Staggered Board* and *Supermajority* provisions that are correlated with *CEO Rep Index* respectively at the 5.86% and 5.64% levels seem to drive such close relation between *CEO Rep Index* and *G-* and *E Index*. This relation indicates that firms run by Republican CEOs, who are politically conservative, prefer a slow-moving board and the voting rule that ensures the continuation of their current organizational structure. This could be interpreted as managerial entrenchment, or a simple reflection of their conservatism in the mode of corporate governance. We examine these issues in a more rigorous empirical set-up in the following sections.

Table 2. Correlations

This table reports pairwise correlations between CEO Republican Index (*CEO Rep Index*) and various corporate governance indices. *CEO Rep Index* is explained in Section 3.1. Corporate governance variables are explained in Section 3.2. *,**, and *** denote the statistical significance at the 10%-, 5%-, and 1%-level, respectively. The sample period is 1996-2006.

		(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
(1)	*CEO Rep Index*	1								
(2)	*G Index*	0.087***	1							
(3)	*E Index*	0.0735***	0.7315***	1						
(4)	*Staggered Board*	0.0586***	0.5094***	0.6306***	1					
(5)	*Limits to Amend Bylaws*	0.0291***	0.3575***	0.4677***	0.2075***	1				
(6)	*Limits to Amend Charters*	0.006	0.1631***	0.2384***	0.0496***	0.1582***	1			
(7)	*Supermajority*	0.0564***	0.2975***	0.3771***	0.1653***	0.108***	0.1172***	1		
(8)	*Golden Parachute*	-0.013	0.3724***	0.5426***	0.1631***	0.0898***	0.0275***	0.0368***	1	
(9)	*Poison Pill*	0.0306***	0.4589***	0.5894***	0.2385***	0.0747***	0.0198**	0.0952***	0.2787***	1

RESULTS

Republican CEOs and external corporate governance

To test the effect of *CEO Rep Index* on the mode of a firm's external corporate governance, we run the following regression for firm-*i* in year-*t*:

$$Governance\ Index_{it} = \alpha_0 + \alpha_1\ CEO\ Rep\ Index_{it} + Controls + \varepsilon_{it}. \quad (2)$$

We use either *G Index* or *E Index* as a firm's external governance index. CEO Republican Index, *CEO Rep Index*, is our main explanatory variable. The expected sign of its point estimate is positive. Control variables include *Board Size*, board *Independence* dummy, *ROA*, *Mkt Lev*, *CF Vol*, and *Log Assets*. We additionally control for year and industry fixed effects, and cluster standard errors at the firm level. Industry is defined using the first two digits of standard industrial classification code (SIC2).

We report the results of this analysis in Table 3. We use *G Index* as our main external governance index in Panel A, whereas *E Index* in Panel B. In column 1 where we include only year and SIC2-level industry fixed effects as control variables, we find the point estimate of 0.314 for *CEO Rep Index*, which is statistically significant at the 1% level. The result indicates that firms run by Republican CEOs tend to adopt governance provisions that shield them from external control change attempts. For a one standard deviation (0.648) increase in *CEO Rep Index*, there is 2.20% (=0.314*0.648/9.259) increase in *G Index* value from its sample average (9.259). When we use *E Index* as our dependent variable in Panel B of the same table, we find the economic magnitude of 3.73% (=0.142*0.648/2.467) increase in *E Index* from its sample average (2.467) for a one standard deviation increase in *CEO Rep Index*. Such economically meaningful effect is also statistically significant at the 1% level.

In column 2 of both panels, we additionally control for firm financial characteristics as well as board characteristics – *Board Size*, *Independence*, *ROA*, *Mkt Lev*, *CF Vol*, *Log Assets*. Despite the inclusion of this long list of additional control variables, the new point estimates of *CEO Rep Index* in both Panel A and B are little changed from their column 1 results.

In column 3, we exclude from our analysis the firm-years where

Table 3. Republican CEO and external corporate governance

The dependent variable is external corporate governance index, either *G Index* by Gompers, Ishii, and Metrick (2003) in Panel A or *E Index* by Bebchuk, Cohen, and Ferrell (2009) in Panel B. CEO Republican Index, *CEO Rep Index*, is used as the main explanatory variable. In column 3, we restrict our sample to firm-years with politically active CEOs, whereas in other columns of this table, we include both politically active and inactive CEO firm-years. *CEO Rep Polarizer* in column 4 takes either 1 (or -1) depending on the CEO being a "pure" Republican (Democratic) Party supporter. Otherwise, the variable takes a value of zero. In column 5, the average Republican Index for a group of outside independent directors is denoted by *ID Rep Index*. In column 6, *CEO Republican (Democrat)* dummy takes a value of one if *CEO Rep Index* > 0 (<0). Control variables include *Board Size*, *Independence* dummy, *ROA*, market leverage ratio (Mkt Lev), cash flow volatility estimated over previous five fiscal years (*CF Vol*), and *Log Assets*. In all columns, year- and two-digit standard industrial classification (SIC2)-level industry-fixed effects are further controlled. In all columns, the standard errors are clustered at the firm level, and t-stats are shown in parentheses. *, **, and *** denote the statistical significance at the 10%-, 5%-, and 1%-level, respectively.

Panel A: *G Index*

VARIABLES	(1) *G Index*	(2) *G Index*	(3) *G Index*	(4) *G Index*	(5) *G Index*	(6) *G Index*
CEO Rep Index	0.314*** (3.568)	0.253*** (2.946)	0.219** (2.466)		0.216** (2.476)	
Board Size		0.159*** (6.485)	0.156*** (5.514)	0.161*** (6.544)	0.159*** (6.458)	0.159*** (6.493)
Independence		0.967*** (7.819)	1.047*** (7.416)	0.975*** (7.839)	0.953*** (7.680)	0.972*** (7.834)
ROA		0.435 (0.758)	0.275 (0.382)	0.486 (0.852)	0.396 (0.693)	0.408 (0.707)
Mkt Lev		1.252*** (2.837)	1.189** (2.264)	1.240*** (2.799)	1.212*** (2.746)	1.246*** (2.823)
CF Vol		-6.881*** (-5.094)	-7.197*** (-4.272)	-6.878*** (-5.106)	-6.836*** (-5.079)	-6.936*** (-5.115)
Log Assets		0.0120 (0.225)	0.00163 (0.0264)	0.0160 (0.299)	0.0130 (0.244)	0.00344 (0.0634)
CEO Rep Polarizer				0.219** (2.316)		
ID Rep Index					0.493** (2.545)	

Table 3. (continued)

VARIABLES	(1) *G Index*	(2) *G Index*	(3) *G Index*	(4) *G Index*	(5) *G Index*	(6) *G Index*
CEO Republican						0.263** (2.055)
CEO Democrat						-0.124 (-0.767)
Constant	9.284*** (103.4)	6.756*** (16.56)	6.828*** (13.99)	6.730*** (16.47)	6.724*** (16.49)	6.776*** (16.63)
Observations	13,055	12,526	9,021	12,526	12,501	12,526
R-squared	0.075	0.132	0.140	0.131	0.134	0.132
Year Fixed Effect	Yes	Yes	Yes	Yes	Yes	Yes
Industry (SIC2) Fixed Effect	Yes	Yes	Yes	Yes	Yes	Yes
Cluster	Firm	Firm	Firm	Firm	Firm	Firm

Panel B: *E Index*

VARIABLES	(1) *E Index*	(2) *E Index*	(3) *E Index*	(4) *E Index*	(5) *E Index*	(6) *E Index*
CEO Rep Index	0.142*** (3.230)	0.136*** (3.150)	0.133*** (2.960)		0.120*** (2.751)	
Board Size		0.0675*** (4.943)	0.0645*** (3.990)	0.0682*** (4.971)	0.0675*** (4.934)	0.0680*** (4.979)
Independence		0.485*** (7.057)	0.511*** (6.318)	0.486*** (7.085)	0.479*** (6.970)	0.486*** (7.073)
ROA		0.0450 (0.146)	0.147 (0.383)	0.0759 (0.247)	0.0350 (0.114)	0.0483 (0.156)
Mkt Lev		0.795*** (3.605)	0.859*** (3.200)	0.787*** (3.563)	0.781*** (3.542)	0.792*** (3.588)
CF Vol		-3.010*** (-4.414)	-3.336*** (-3.893)	-3.007*** (-4.419)	-2.964*** (-4.360)	-3.049*** (-4.473)
Log Assets		-0.151*** (-5.711)	-0.179*** (-5.843)	-0.149*** (-5.604)	-0.151*** (-5.737)	-0.153*** (-5.695)
CEO Rep Polarizer				0.116** (2.446)		

Table 3. (continued)

VARIABLES	(1) *E Index*	(2) *E Index*	(3) *E Index*	(4) *E Index*	(5) *E Index*	(6) *E Index*
ID Rep Index					0.226** (2.280)	
CEO Republican						0.105* (1.647)
CEO Democrat						-0.0934 (-1.169)
Constant	2.239*** (48.45)	2.261*** (11.15)	2.485*** (10.12)	2.251*** (11.07)	2.243*** (11.08)	2.274*** (11.23)
Observations	11,696	11,258	8,131	11,258	11,243	11,258
R-squared	0.090	0.133	0.149	0.131	0.135	0.132
Year Fixed Effect	Yes	Yes	Yes	Yes	Yes	Yes
Industry (SIC2) Fixed Effect	Yes	Yes	Yes	Yes	Yes	Yes
Cluster	Firm	Firm	Firm	Firm	Firm	Firm

CEOs are politically inactive. We find that our earlier results are not biased by the inclusion of these politically inactive CEOs whose Republican Index values are coded to be zero. The new point estimates of *CEO Rep Index* in column 3 are almost identical to the estimates in column 2 of both panels.

Next in column 4, we test whether our results are driven by political polarizers whose political views are either right- or left-extreme, or they are driven by modest Republican or Democratic CEOs whose donations sometimes go to the opposite political party to the one they primarily support. In this test, we assign 1 (or -1) to only "pure" Republican (or Democrat) who donate to only the Republican (or Democratic) Party throughout the whole election cycles. For other CEOs, we assign zero values. We include politically inactive CEOs in this analysis. Using this polarized Republican Index, we find 0.219 in Panel A, a positive and statistically significant point estimate for *CEO Rep Polarizer*, at the 5% level. Similar positive (0.116) and significant results (5% level) are found in

Panel B where we use *E Index* on the LHS of our regression. These results assure that our results are indeed driven by strong, bi-partitioned political values among politically active CEOs. In column 5 of both panels, we show that such significant *CEO Rep Index* effects on external governance indices are not confounded with the Republican Index of the group of independent directors on the board (*ID Rep Index*).

As we find strong political value influences on a firm's external governance choices, a natural question is then – Do Republican CEOs drive such strong relation between their political value and the firm's external governance index, or Democratic CEOs? To see which side of political values drives our results, we create *CEO Republican* (*CEO Democrat*) dummy, which takes a value of 1 (-1) for CEOs whose *CEO Rep Index* values are strictly positive (negative). The overall constant of our regression, therefore, captures the effect of CEOs who are either politically inactive or supporting for both political parties with equal donation amounts. Using these dummy variables, we re-run our column 2 regression analyses.

The results are reported in column 6 of both Panel A and B. We find that 0.263 (0.105) as our point estimate for *CEO Republican* dummy in Panel A (Panel B), which is statistically significant at the 5% (10%) level. However, we do not find significant effect of *CEO Democrat* dummy in both panels, although the sign of their point estimates are in line with our earlier findings when we use *CEO Rep Index* as our main explanatory variable. From these results, we conclude that poor external governance of a firm measured by *G* and/or *E Index* is primarily driven by Republican CEOs rather Democratic CEOs.

In summary, our results in Table 3 are consistent with our proposition on the corporate governance conservatism of Republican CEOs. However, our results do not necessarity exclude the potential managerial entrenchment of these politically conservative CEOs. We will conduct further analyses to sharply identify the corporate governance conservatism rather than the managerial entrenchment in the later Section 4.2.

Republican CEO and each corporate governance provision in G- and E Index Next, we further investigate which governance provision in *G*- and *E Index* is more or less likely to reflect the CEO's political conservatism. As explained in Section 3.2, there are 24 governance

provisions in *G Index*, and six provisions among them are separately included in *E Index* because Bebchuk, Cohen, and Ferrell (2009) find these six provisions most closely related to the entrenchment discount. In our analysis, we consider all of these six *E Index* constituent provisions as well as two other compensation-related provisions that are exclusively included in *G Index* (*Compensation Plan* and *Severance*).

As stability and continuity are preferred by the conservatives, we expect *Staggered Board* provision in the Delay category would be particularly preferred by the Republican top managers. Three provisions in the Voting category would equally help Republican CEOs achieve stable and continuous organizational structure. Among them, *Supermajority* also minimizes the possibility of ambiguous voting outcomes, which is in line with the conservatives' high demand for cognitive closure. Hence, *ceteris paribus*, we expect a particularly strong correlation between *Supermajority* and the CEO's Republican status among the governance provisions in the Voting category.

Golden Parachute from the Protection category and *Poison Pill* from the Other category would also help Republican managers protected from external control change events. However, the former, *Golden Parachute*, could be against the conservatives' personal norm on hard working and self-disciplining culture. This could possibly lead to a weak correlation between *Golden Parachute* and *CEO Rep Index.*

With all these backgrounds, we run our baseline regression as specified in Eq. (2), while we vary our dependent variable from *Staggered Board* dummy to *Poison Pill* dummy. The results are reported in columns 1 to 6 of Table 4.

We find significant and positive point estimates of *CEO Rep Index* for the following three governance provisions – *Staggered Board* (column 1), *Limits to Amend Bylaws* (column 2), and *Supermajority* (column 4). Overall we find positive correlations between each governance provision in *E-Index* and *CEO Rep Index*, although *Limits to Amend Charter* dummy (column 3) and *Golden Parachute* dummy (column 5) show an insignificant and negative relation with *CEO Rep Index*.

We are interested in whether our result on *Golden Parachute* dummy (column 5) could indicate the existence of the strong self-disciplining culture among Republican CEOs. If true, we expect such evidence exists for other governance provisions that are specifically

Table 4. Republican CEO and each corporate governance provision in *G*- and *E Index*

The dependent variable is each corporate governance provision in both *E* and *G Index* (columns 1 to 6) or included in G Index only (columns 7 to 8). See Section 3.2 for the definition of each corporate governance provision. CEO Republican Index, *CEO Rep Index*, is used as the main explanatory variable. Control variables include *Board Size, Independence* dummy, *ROA, m*arket leverage ratio (*Mkt Lev*), cash flow volatility estimated over previous five fiscal years (*CF Vol*), and *Log Assets*. In all columns, year- and two-digit standard industrial classification (SIC2)-level industry-fixed effects are further controlled. In all columns, the standard errors are clustered at the firm level, and t-stats are shown in parentheses. *, **, and *** denote the statistical significance at the 10%-, 5%-, and 1%-level, respectively.

VARIABLES	(1) Staggered Board	(2) Limits to Amend Bylaws	(3) Limits to Amend Charter	(4) Supermajority	(5) Golden Parachute	(6) Poison Pill	(7) Compensation Plan	(8) Severance
CEO Rep Index	0.0351**	0.0210*	-0.00179	0.0275**	-0.00434	0.0104	-0.00682	-0.00967
	(2.178)	(1.665)	(-0.352)	(2.213)	(-0.314)	(0.697)	(-0.557)	(-1.317)
Board Size	0.0134***	0.00612	0.00326**	0.00699**	0.00899**	0.0121***	0.00861**	0.000505
	(2.977)	(1.625)	(2.070)	(2.018)	(2.169)	(2.812)	(2.307)	(0.203)
Independence	0.0739***	-0.0120	0.00736	0.0371**	0.220***	0.253***	0.132***	-0.0464***
	(3.035)	(-0.625)	(0.979)	(2.112)	(9.815)	(11.34)	(5.607)	(-3.017)
ROA	0.0324	-0.0536	-0.0262	0.0399	0.0133	-0.0910	0.0262	-0.0755
	(0.264)	(-0.714)	(-0.962)	(0.492)	(0.130)	(-0.819)	(0.261)	(-1.154)
Mkt Lev	0.106	0.0861	0.00825	0.0523	0.391***	0.193**	0.164**	-0.0944**
	(1.240)	(1.342)	(0.370)	(0.802)	(5.426)	(2.569)	(2.271)	(-2.322)
CF Vol	-1.060***	0.0357	-0.0323	-0.896***	-0.0850	-0.248	-0.270	0.174
	(-3.691)	(0.174)	(-0.545)	(-4.934)	(-0.367)	(-0.967)	(-1.136)	(1.230)

Table 4. (continued)

VARIABLES	(1) Staggered Board	(2) Limits to Amend Bylaws	(3) Limits to Amend Charter	(4) Supermajority	(5) Golden Parachute	(6) Poison Pill	(7) Compensation Plan	(8) Severance
Log Assets	-0.0372***	-0.00221	-0.00421	-0.0168**	-0.0229***	-0.0268***	0.0305***	0.00226
	(-3.774)	(-0.298)	(-1.516)	(-2.349)	(-2.816)	(-2.899)	(3.548)	(0.534)
Constant	0.685***	0.0915*	0.0173	0.204***	0.368***	0.434***	0.272***	0.140***
	(9.055)	(1.668)	(0.860)	(3.845)	(5.541)	(6.122)	(4.091)	(3.712)
Observations	12,526	12,526	12,526	12,526	12,526	12,526	12,526	12,526
R-squared	0.076	0.052	0.034	0.063	0.139	0.096	0.084	0.052
Year F.E.	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Industry F.E.	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Cluster	Firm	Firm	Firm	Firm	Firm	Firm	Firm	Firm

related to their personal pays. Hence in the remaining columns 7 to 8 of Table 4, we use two additional compensation-related provisions that are exclusively included in *G-Index*. There we find consistent results – a negative correlation between *Compensation Plan*/ *Severance* and *CEO Rep Index*.

Overall, our results in Table 4 further confirm that corporate governance conservatism exists among firms run by Republican mangers at the individual governance provision level.

Robustness to other CEO characteristics One could argue that omitted personal characteristics of CEOs could drive our results. To show that our results are robust to this concern, in Table 5, we introduce various CEO personal characteristics as additional control variables in our regressions. In Panel A of this table, we use *G Index* as our dependent variable, whereas we use *E Index* in Panel B of the same table.

In column 1 of both panels of Table 5, we employ the regression specification we used in column 2 of Table 3, while we additionally control for *CEO age*. Neither the regression R-squared nor the point estimate of *CEO Rep Index* is changed much from the result reported in column 2 of Table 3. We continue to find a similar robustness of our baseline results to the additional *Female CEO* (dummy) control variable in column 2 of both panels.

In column 3 of Table 5, we control for *CEO Tenure*. Our results are still robust to this additional control variable. *CEO Tenure* significantly explains a lower *G*- and *E Index* values, which implies that well-established CEOs are far from being entrenched. Next in columns 4 and 5 of Panel A and B, we respectively control for *CEO Chairman (dummy)* and *CEO Stock Holding (%)* as additional control variables. None of the two additional control variables changes our baseline results. High CEO stock holding could be a positive signal for the quality of corporate governance (Jensen and Meckling, 1976). We indeed find a significant and negative correlation between *CEO Stock Holding (%)* and external governance indices in column 5 of both panels.

Overall, our results in Table 5 alleviate concerns about omitted CEO personal characteristics that could be confounded with *CEO Rep Index* effects. Such confounding factors do not seem to drive our results.

Table 5. Robustness to other CEO characteristics

This table shows the robustness of Table 3 results to the following additional CEO characteristic controls: *CEO Age* in column 1, CEO gender (*Female CEO* dummy) in column 2, *CEO Tenure* in column 3, CEO is a board chairman (*CEO Chairman dummy*) in column 4, and *CEO Stock Holding (%)* in column 5. In all columns, year- and two-digit standard industrial classification (SIC2)-level industry-fixed effects are further controlled. In all columns, the standard errors are clustered at the firm level, and t-stats are shown in parentheses. *, **, and *** denote the statistical significance at the 10%-, 5%-, and 1%-level, respectively.

Panel A: *G Index*

VARIABLES	(1) *G Index*	(2) *G Index*	(3) *G Index*	(4) *G Index*	(5) *G Index*
CEO Rep Index	0.264*** (3.015)	0.251*** (2.904)	0.258*** (2.967)	0.249*** (2.879)	0.246*** (2.862)
CEO Age	-0.0102 (-1.594)				
Female CEO (dummy)		-0.238 (-0.532)			
CEO Tenure			-0.0332*** (-4.425)		
CEO Chairman (dummy)				0.245 (1.161)	
CEO Stock Holding (%)					-0.0581*** (-5.828)
Board Size	0.158*** (6.406)	0.159*** (6.467)	0.151*** (6.032)	0.159*** (6.485)	0.138*** (5.501)
Independence	0.965*** (7.690)	0.969*** (7.842)	0.919*** (7.266)	0.963*** (7.762)	0.784*** (6.288)
ROA	0.447 (0.760)	0.428 (0.747)	0.404 (0.694)	0.428 (0.748)	0.398 (0.687)
Mkt Lev	1.211*** (2.716)	1.250*** (2.833)	1.088** (2.432)	1.253*** (2.837)	1.122** (2.544)
CF Vol	-7.512*** (-5.554)	-6.872*** (-5.088)	-7.620*** (-5.630)	-6.841*** (-5.059)	-7.381*** (-5.502)
Log Assets	0.0177 (0.327)	0.0120 (0.224)	-0.0203 (-0.374)	0.0118 (0.221)	0.00525 (0.0982)
Constant	7.313*** (13.70)	6.762*** (16.59)	7.469*** (17.61)	6.521*** (13.86)	7.338*** (17.44)
Observations	11,876	12,526	11,789	12,526	11,841
R-squared	0.135	0.133	0.141	0.133	0.144
Year Fixed Effect	Yes	Yes	Yes	Yes	Yes
Industry (SIC2) Fixed Effect	Yes	Yes	Yes	Yes	Yes
Cluster	Firm	Firm	Firm	Firm	Firm

Table 5. (continued)

Panel B: *E Index*

VARIABLES	(1) *E Index*	(2) *E Index*	(3) *E Index*	(4) *E Index*	(5) *E Index*
CEO Rep Index	0.139*** (3.166)	0.135*** (3.134)	0.132*** (3.009)	0.133*** (3.091)	0.127*** (2.960)
CEO Age	-0.00568* (-1.718)				
Female CEO		-0.0378 (-0.175)			
CEO Tenure			-0.0152*** (-4.206)		
CEO Chairman (dummy)				0.146 (1.549)	
CEO Stock Holding (%)					-0.0358*** (-7.262)
Board Size	0.0666*** (4.841)	0.0674*** (4.934)	0.0593*** (4.332)	0.0674*** (4.935)	0.0529*** (3.864)
Independence	0.487*** (6.945)	0.485*** (7.065)	0.445*** (6.637)	0.481*** (6.975)	0.388*** (5.629)
ROA	0.0823 (0.259)	0.0442 (0.143)	-0.0335 (-0.107)	0.0389 (0.126)	0.120 (0.384)
Mkt Lev	0.819*** (3.687)	0.795*** (3.603)	0.741*** (3.318)	0.795*** (3.609)	0.789*** (3.599)
CF Vol	-3.238*** (-4.724)	-3.007*** (-4.408)	-3.177*** (-4.638)	-2.989*** (-4.379)	-3.264*** (-4.798)
Log Assets	-0.149*** (-5.560)	-0.151*** (-5.711)	-0.153*** (-5.741)	-0.151*** (-5.723)	-0.160*** (-6.044)
Constant	2.567*** (9.444)	2.262*** (11.14)	2.560*** (12.09)	2.125*** (9.586)	2.624*** (12.61)
Observations	10,659	11,258	10,646	11,258	10,634
R-squared	0.137	0.133	0.135	0.133	0.148
Year Fixed Effect	Yes	Yes	Yes	Yes	Yes
Industry (SIC2) Fixed Effect	Yes	Yes	Yes	Yes	Yes
Cluster	Firm	Firm	Firm	Firm	Firm

Conservatism or managerial entrenchment?

As emphasized earlier, corporate governance conservatism is well-identified if poor external governance practices do not lead

to any entrenchment discount in corporate value. To ensure that our findings in Table 3 to 5 are truly reflecting the conservative attitudes of Republican top managers rather than their managerial entrenchment, we run several value and financial conservatism regressions as conducted in the existing studies (Yermack, 1996; Bebchuk, Cohen, and Ferrell, 2009; Hutton, Jiang, and Kumar, 2014; Lee, Lee, and Nagarajan, 2014, among others). We show that *CEO Rep Index*, while controlling for *G-* and *E Index*, results in neither a lower firm value (*Q*) nor lower operating efficiency (*ROA*). Instead, consistent with Hutton, Jiang, and Kumar (2014), we show that corporate leverage policies are conservatively taken by Republican top managers.

Table 6 reports these results. In the first three columns of the table, we control for *G Index* on the right-hand-side (RHS) of the regressions. In the next three columns of the table, we control for *E Index*. Column 1 and 4 of Table 6 show the valuation (*Q*) results. We follow the regression specification used by Yermack (1996) and Lee, Lee, and Nagarajan (2014), while we use *CEO Rep Index* as our main explanatory variable. In both columns 1 and 4, we find no significant evidence of managerial entrenchment for firms run by Republican top managers. We obtain positive, statistically insignificant, point estimates of *CEO Rep Index* in both columns.

In columns 2 and 5 of Table 6, we test for operating efficiency of firms run by Republican CEOs. There we find the positive point estimates of *CEO Rep Index* at the 1% statistical significance. The results indicate that Republican CEOs, although they adopt corporate governance provisions in a way to shield themselves from external disciplining mechanisms, still efficiently manage their corporations. These results are consistent with Hutton, Jiang, and Kumar (2014), although our regression specification includes a broader set of firm financial variables than that used by Hutton, Jiang, and Kumar (2014).

Lastly, in columns 3 and 6 of the same table, we find the conservative use of corporate leverage for firms run by Republican managers. This is also in line with the economic, financial conservatism of Republican CEOs that is proposed and reported by Hutton, Jiang, and Kumar (2014).

Overall, our results in Table 6 establish an important notion of corporate governance conservatism among firms run by Republican top managers. Despite seemingly-problematic external governance

Table 6. Conservatism or entrenchment?

This table shows valuation (columns 1 and 4), operating efficiency (columns 2 and 5), and market leverage (columns 3 and 6) results. The dependent variables are Tobin's *Q* in columns 1 and 4, *ROA* in columns 2 and 5, and *Mkt Lev* in columns 3 and 6. Main explanatory variable is *CEO Rep Index*. Main control variables are *G Index* (columns 1 to 3) and *E Index* (columns 4 to 6). Other control variables include *Board Size, Independence* dummy, investment intensity (*INV*), research and development expenses to assets (*R&D*), cash flow volatility estimated over previous five fiscal years (*CF Vol*), and *Log Assets*. In all columns, year- and two-digit standard industrial classification (SIC2)-level industry-fixed effects are further controlled. In all columns, the standard errors are clustered at the firm level, and t-stats are shown in parentheses. *, **, and *** denote the statistical significance at the 10%-, 5%-, and 1%-level, respectively.

VARIABLES	(1) *Q*	(2) *ROA*	(3) *Mkt Lev*	(4) *Q*	(5) *ROA*	(6) *Mkt Lev*
CEO Rep Index	0.0326 (0.989)	0.00747*** (3.155)	-0.00715* (-1.878)	0.0487 (1.389)	0.00856*** (3.427)	-0.00900** (-2.287)
G Index	-0.0179** (-2.189)	-5.64e-05 (-0.0976)	0.00199** (2.079)			
E Index				-0.0718*** (-3.996)	-0.00124 (-0.975)	0.00574*** (2.922)
Board Size	-0.00363 (-0.414)	0.000780 (1.291)	-0.00237** (-2.217)	-0.00270 (-0.297)	0.000499 (0.783)	-0.00235** (-2.119)
Independence	-0.0491 (-0.874)	0.00396 (1.025)	-0.000150 (-0.0241)	-0.0533 (-0.854)	0.00254 (0.587)	-0.00204 (-0.313)
INV	2.043*** (10.99)	0.113*** (9.329)	-0.147*** (-9.384)	2.078*** (10.42)	0.111*** (8.578)	-0.153*** (-9.929)
RND	5.500*** (5.959)	-0.348*** (-4.635)	-0.487*** (-8.581)	5.583*** (5.864)	-0.334*** (-4.391)	-0.486*** (-8.466)
CF Vol	2.539*** (2.620)	-0.405*** (-4.916)	0.209*** (2.931)	2.315** (2.414)	-0.431*** (-5.177)	0.238*** (3.162)
Log Assets	0.0573** (2.560)	-0.00115 (-0.725)	0.0142*** (5.631)	0.0489** (2.109)	-0.00120 (-0.724)	0.0143*** (5.727)
Constant	0.997*** (5.690)	0.141*** (11.43)	0.0955*** (5.082)	1.044*** (5.593)	0.147*** (11.46)	0.103*** (5.454)
Observations	12,585	12,559	12,553	11,307	11,286	11,280
R-squared	0.285	0.269	0.381	0.299	0.279	0.401
Year Fixed Effect	Yes	Yes	Yes	Yes	Yes	Yes

Table 6. (continued)

VARIABLES	(1) *Q*	(2) *ROA*	(3) *Mkt Lev*	(4) *Q*	(5) *ROA*	(6) *Mkt Lev*
Industry (SIC2) Fixed Effect	Yes	Yes	Yes	Yes	Yes	Yes
Cluster	Firm	Firm	Firm	Firm	Firm	Firm

structure, firms run by these politically conservative managers do not suffer from any significant entrenchment discount. That said, their choices of governance provisions rather reflect the conservative attitudes of Republican CEOs. This is consistent with our theory developed in Section 2.

FURTHER DISCUSSIONS ON CORPORATE GOVERNANCE CONSERVATISM

Though this paper has focused on the implication of top manager's political conservatism for external governance provisions, there is another important dimension of corporate governance practice which could potentially be affected by political conservatism – *board diversity*.

There is a growing interest in board diversity in recent years (Adams and Ferreira, 2004, 2009; Rhode and Packel, 2010; Masulis, Wang, and Xei, 2012; Lee, Lee, and Nagarajan, 2014). For instance, a 2012 survey of U.S. corporate board members indicates that three-fourths of respondents indicated that their company had taken steps to support and promote boardroom diversity efforts in the past three years. In spite of various efforts to achieve boardroom diversity in the U.S. firms, the vast majority of corporate directors still belong to a certain demographic group in terms of age, gender and race. For example, a study on the directors who were at Fortune 500 companies in 2011 shows that 87.2% of them are whites and 84.5% of them are male.[10)]

10) Richard L. Zweigenhaft, http://www2.ucsc.edu/whorulesamerica/power/diversity_among_ceos.html.

Our theory of corporate governance conservatism suggests that top managers' political conservatism might be a deterrent to boardroom diversity, especially when they can influence the nomination and appointment of new directors. Conservative CEOs, who are resistant to change and averse to equality, may want to avoid diversity within the board and fill vacant board seats with people from more homogenous backgrounds to themselves. We believe there will be a strong, negative correlation between CEOs' political conservatism and boardroom diversity in the U.S. private sectors. Given the increasing attention to the board diversity and boardroom culture, fruitful future research opportunities seem to lie ahead along this direction.

CONCLUSIONS

In this paper, we develop a novel definition of "corporate governance conservatism," which reflects the preference of politically conservative CEOs for stability and continuity in the corporate governance structure. The important condition behind this corporate governance conservatism is that despite the resulting seemingly-poor external governance practices, strong internal governance of politically conservative top managers prevents the usual managerial entrenchment problems. Thus, under the corporate governance conservatism, shareholders should not suffer from entrenchment discounts in their value in spite of more frequently adopted governance provisions that insulate top managers from external disciplining mechanisms.

We find strong empirical support for our hypothesis. Using 2,339 U.S. corporations from 1996 to 2006 we find that firms run by Republican CEOs, who are politically conservative, are more likely to adopt staggered boards, limits to amend bylaws, and supermajority provisions, but these CEOs do not run their firms in inefficient ways. We rather find evidence of financial conservatism of Republican CEOs, which is consistent with the notion introduced by Hutton, Jiang, and Kumar (2014).

We believe that our results highlight an important spillover effect of the CEO political conservatism on corporate governance choices. CEOs' personal traits such as their personal value systems shape the mode of corporate governance. Here we are limited to show

the evidence of such CEO effects on external governance choices. However, there could be other important applications of our theory. We discuss the board diversity as one of such applications. We predict that conservative top managers avoid diverse boards in terms of directors' age, ethnic, and gender backgrounds. Given the increasing attention to the board diversity and boardroom culture in recent years, we believe that fruitful future research opportunities lie ahead along this direction.

Appendix. Financial variable definitions using Compustat variable names

	Definition
ROA	The ratio of operating income before depreciation (OIBDP) to the book value of a firm's total assets (AT).
Q	Average Tobin's *Q*, which is the ratio of market value of a firm's total assets to their book value. The market value of a firm's assets is computed as the book value of a firm's total assets (AT) minus the book value of common equity plus market value of common equity (PRCC_F*CSHO) minus deferred taxes and investment credits (TXDITC) (if available). The book value of common equity is computed as the total stockholders' equity (SEQ) [or, if this is missing, the first available of total common equity (CEQ) plus total preferred stock (PSTK) or total assets (AT) minus total liabilities (LT)] minus the liquidating value of preferred stock (PSTKL) [or, if that is missing, the first available of the redemption value of preferred stock (PSTKRV) or total preferred stock (PSTK)].
INV	The ratio of capital expenditure (CAPX) to total net property, plant, and equipment (PPENT). For a missing CAPX, we replace it with zero.
R&D	The ratio of research and development expense (XRD) to the book value of a firm's total assets (AT). For a missing XRD, we replace it with zero.
Mkt Lev	The ratio of the book value of total debt (DLC+DLTT) to the market value of a firm's total assets. See the definition of *Q* above for the definition of the market value of a firm's total assets.
CF Vol	The cash flow (oibdp/at) volatility measured over past five years.
Log Assets	The natural logarithm of the inflation-adjusted book value of a firm's total assets (AT/Average annual consumer price index (CPI)). CPI is normalized to be one for the year 1992.

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