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## Abstract

We find evidence suggesting that similarity of political views between the CEO and independent directors ("political homophily") encourages the CEO to share adverse information with the board. Firms with higher political homophily have lower stock price crash risk, are more likely to divest previously acquired assets with poor announcement returns, and write down loss-making assets. Furthermore, the effect of political homophily is complemented by strong shareholder governance which prevents friendly board from insulating the CEO in the case of ex post negative outcomes. Our identification utilizes the exogenous variation in political beliefs associated with the entry of a conservative television network in local markets. Our findings show that a friendly board facilitates CEO-board communication which is crucial for the board to function effectively in its advisory role.

Keywords: friendly board, CEO-board communication, political homophily, crash risk, corporate governance

JEL Classifications: D72, G32, G34, G41, M12, M14

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# Similarity Breeds Trust: Political Homophily and CEO-Board Communication


## Abstract

We find evidence suggesting that similarity of political views between the CEO and independent directors ("political homophily") encourages the CEO to share adverse information with the board. Firms with higher political homophily have lower stock price crash risk, are more likely to divest previously acquired assets with poor announcement returns, and write down loss-making assets. Furthermore, the effect of political homophily is complemented by strong shareholder governance which prevents friendly board from insulating the CEO in the case of *ex post* negative outcomes. Our identification utilizes the exogenous variation in political beliefs associated with the entry of a conservative television network in local markets. Our findings show that a friendly board facilitates CEO-board communication which is crucial for the board to function effectively in its advisory role.



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The willingness of a privately informed CEO to share adverse information with the corporate board has major implication for shareholder value. The common adage about "a stitch in time" applies for corporate decision making: timely corrective actions are likely to limit future losses. When a CEO has private information that an existing project is value-destroying and would likely lead to a large loss to the company, she needs to decide whether to take a chance (e.g., wait for improved external environment or explore opportunities elsewhere by "jumping a sinking ship") or take corrective actions. The latter choice can reduce the likelihood of a large loss and stock price crash risk, but for corrective actions to happen, the CEO typically needs to inform the board, and sometimes seek its approval (for example, for major corporate decisions such as divesting loss-making assets). An important constraint is that revealing adverse information to the board may reflect negatively on the CEO's own past performance and credibility with the board.[1] Not much is known, however, as to what may overcome this constraint and facilitate the sharing of negative information.

In this paper, we study the role of a "friendly board" in facilitating the CEO's communication of negative information with the board. Our approach is motivated by the recent literature on sociology and politics suggesting that similar political views promote homophily, i.e., trust and bonding among individuals.[2] To this end, we examine if the more congruent political ideologies of the CEO and the independent directors facilitate the sharing of information, especially adverse information, and in turn reduce the later incidence of significant adverse outcomes and stock price crash risk.

Our research question is closely related to, but distinct from, the theoretical arguments

[1] For example, Boot (1992) proposes a model in which managers of low ability may not divest underperforming assets because of the reputational costs.
[2] See, for example, McPherson, Smith-Lovin, and Cook (2001), Huber and Malhotra (2017), and Banda, Carsey and Severenchuk (2020). Section 1 discusses the details of these findings.

about a friendly board. For example, in Adams and Ferreira's (2007) model, a friendly board provides the advisory benefit from sharing information while refraining from monitoring the CEO intensively or limiting her private benefits.[3] Our research question complements the existing literature on both the advisory and the monitoring roles of a friendly board. Regarding the advisory role, while our hypothesis also assumes a smooth communication between the CEO and the friendly board, we do not require the board to necessarily "advise" the CEO on the shared negative information. Regarding the monitoring role, our hypothesis also assumes less strict monitoring (and more trust) by the friendly board. Such leniency becomes beneficial when the CEO needs to take corrective actions. Nonetheless, since our setting is subsumed in the broader notion of board friendliness and provides important evidence on its key tenets, we refer to a board that has a high degree of political homophily with the CEO as a "friendly board" throughout this paper.

Our sample consists of 26,376 firm-years between 1999 and 2019. Each firm-year has an average of 7.6 independent directors. We construct a measure of CEO-board political homophily, *Political Homophily Index* (henceforth *PHI*), based on political contributions made by the CEO and independent directors to political committees/candidates during the previous election cycle. Using such contributions as a "revealed preference" measure of an individual's political orientation, *PHI* captures, in the U.S. bipartisan setup, the extent to which the CEO and the "average" independent director of a firm have similar political views.[4]

We first examine the relationship between *PHI* and the firm's stock price crash risk. Previous studies show that, given information asymmetry between corporate insiders and outside

[3] In Adams and Ferreira's (2007) model, the board's monitoring intensity is a function of its monitoring cost, which could be determined by board composition (e.g., the degree of board independence). The key result is that there could be an (interior) optimal degree of board independence which balances the monitoring and advisory roles.
[4] The similarity measure is the Euclidean distance between the political orientation of the CEO and the average political orientation of independent directors.

investors, accumulation of negative private information can cause stock price crashes when such negative information is revealed (e.g., Jin and Myers, 2006; Hutton, Marcus, and Tehranian, 2009). If political homophily facilitates the CEO's sharing of negative information and therefore helps address the firm's problems in a timely manner, then high *PHI* firms will have a lower likelihood of a large unexpected loss and in turn a lower stock price crash risk. We follow the literature and construct two measures of a firm's stock price crash risk: one-year ahead negative skewness, and asymmetric (down-to-up) volatility of daily stock returns (e.g., Chen, Hong, and Stein, 2001; Kim, Li, and Zhang, 2011a, 2011b; Callen and Fang, 2015; DeFond et al., 2015; Kim and Zhang, 2016; Xu, Xuan, and Zheng, 2021; Hsu, Wang, and Whipple, 2022).

To test our hypothesis, we estimate panel regressions of crash risk measures on *PHI* which control for a broad set of firm level characteristics. Consistent with our prediction, we find that the coefficient of *PHI* is negative and statistically significant at the 1% level in the regressions of both crash risk measures. For robustness, we follow the literature and construct four alternative measures of political homophily based on alternative measurement windows or alternative selections of contributions, and our regression results remain very similar using these alternative measures. In addition, we include the average Republican index of a firm's directors as an additional control variable in the baseline regressions and find that the economic and statistical significances of the coefficients on *PHI* are not affected, suggesting that our results are driven by political homophily rather than Republican orientation of the board. These results indicate that, consistent with friendly board facilitating CEO-board communication of negative information, political homophily is negatively associated with future stock price crash risk.

We acknowledge that reverse causality or omitted variables might drive the observed negative relationship between a firm's political homophily and stock price crash risk. For example,

firms with lower crash risk might affect board homophily via endogenous changes in board composition. To address endogeneity concerns, we utilize exogenous variation in political beliefs associated with the entry of the Sinclair Broadcast Group, the largest U.S. local television station operator, into different U.S. regions. Starting in the 1980s, Sinclair has expanded mostly via acquisitions of local television stations across the states. Sinclair has a strong conservative orientation, and it often broadcasts news that is in favor of and favored by the Republicans (Martin and McCrain, 2019).

Consistent with the literature that people's political views can be significantly affected by public media and propaganda (e.g., DellaVigna and Kaplan, 2007; Durante, Pinotti, and Tesei, 2019), we find evidence that Sinclair's entry into a county significantly shifts the local directors' political leaning towards the Republican party.[5] Therefore, we explore the exogenous variation in *PHI* caused by the Sinclair acquisitions and its impact on firms' crash risk using a three-step procedure following Adams, Almeida, and Ferreira (2009). Specifically, in the first stage, we estimate the impact of Sinclair acquisitions on directors' political views at the individual-director level. In the second stage, we compute the political homophily index using individual directors' Republican indices predicted in the first stage (*PHISinclair*). In the third stage, we estimate our baseline model using *PHISinclair* as the instrument for *PHI*. We find that the negative relation between political homophily and future crash risk remains robust with this approach.

To investigate the channels through which the CEO-Board political homophily reduces crash risk, we conduct two analyses to test if political homophily promotes information sharing and leads to corrective actions being implemented in a timely manner. Our test of information

[5] In contrast, the Sinclair entry does not have a significant impact on CEOs' political leaning. This is the possibly due to the fact that CEOs are ex ante already much more Republican-oriented than the directors, and that CEO overconfidence (e.g., Malmendier and Tate, 2005, 2008) makes CEOs update their beliefs to a lesser degree than directors in response to media.

sharing is motivated by Ravina and Sapienza's (2010) finding that the insider purchases by independent directors earn positive abnormal returns but such returns are lower relative to executives' insider purchases. This suggests that executives possess more private information than independent directors. We find that when there is higher political homophily, independent directors' insider purchases become more profitable, and the performance gap with the executives' insider purchases narrows. This result is consistent with the premise that political homophily encourages CEOs to share more private information with directors.

We further conduct two tests of corrective actions. First, we examine divestitures of previously acquired assets with poor performance. We follow the literature and use firms' acquisition announcement returns to measure performance, and find that acquired assets with poor performance are more likely to be divested subsequently when political homophily is higher. This result is consistent with the premise that political homophily increases managers' incentives to take corrective actions and avoid further losses. Second, we follow the methodology of Lawrence, Sloan, and Sun (2013) and show that political homophily increases managers' likelihood of recognizing losses via asset write-downs.

Finally, we examine whether the positive effect of a friendly board on CEO-board communication relies on strong shareholder governance. When shareholder governance is weak, the CEO will be reasonably assured that she would enjoy downside protection from a friendly board even if negative outcomes occurred because timely actions were not taken. In such a scenario, political homophily need not lead to more information sharing. However, when shareholder governance is strong and external pressure is high, even a friendly board will not be able to protect the CEO's job upon a large loss. Therefore, we expect that strong external governance, and in particular, strong shareholder governance, is essential for a friendly board to

facilitate the communication of negative information. In this case, the friendly board acts as a complement to shareholder governance.

We follow the literature and construct two commonly used indicators of shareholder governance – ownership by institutional investors (e.g., Denis, Denis, and Sarin, 1997; Harford, Jenter, and Li, 2011), and the E-Index (Bebchuk, Ferrell, and Cohen, 2009). We first show that, consistent with Lee, Lee, and Nagarajan (2014), for our overall sample, the negative relationship between CEO turnover and past performance is absent when political homophily is high, which is consistent with a friendly board offering downside protection to the CEO. However, we find that this downside protection effect only holds in subsamples where shareholder governance is weak. Homophily has no weakening effect on turnover-performance sensitivity when shareholder governance is strong.

We further examine the interactive effect of *PHI* and shareholder governance on stock price crash risk. We find that the negative relationship between political homophily and stock price crash risk is concentrated in the subsamples where shareholder governance is strong but disappears in the subsamples where shareholder governance is weak. This result, together with the results on CEO turnover, suggest that the effect of a friendly board on CEO-board communication relies on strong shareholder governance.

We make several contributions to the literature. First, while existing literature has investigated the dual monitoring and advisory roles of boards, there is limited evidence on which board attributes encourage more information sharing by the CEO. With the exception of Adams (2010), who provides survey evidence that independent directors receive less strategic information from the management when they monitor more intensively, we are not aware of any paper that directly examines the key idea that by committing to less intensive monitoring, a friendly board

can encourage more information sharing. Under the presumption that political homophily promotes more trust and tolerance of negative outcomes (at least as long as they are brought promptly to the board's attention), our results provide evidence on this very important aspect of the theory.

Second, in tandem with Lee, Lee, and Nagarajan (2014), who document that political homophily between the CEO and the board weakens the board's monitoring role, we show that political homophily encompasses both the features of the friendly board theory – monitoring and information sharing. While we do not explicitly consider the board's advisory role, we suggest a new benefit of sharing negative information – the ability to take timely actions to avert even worse consequences in the future. Further, our results suggest that when the CEO is considering revealing negative information to the board – be it for the board's advice or just to seek the board's support for timely, corrective actions – the homophily measure may have some advantage over other measures, such as social connections between the CEO and members for the board. This is because when the information is negative, the CEO must trust the entire board not to take actions against herself. However, Schmidt (2015) reports that only 4% of board members, on average, are connected to the CEO via social ties, and another 4% via employment ties. Such weak ties may not provide the CEO with the tolerance she needs.

Furthermore, we show that shareholder governance can complement the role played by a friendly board. When the board is friendly, stronger shareholder governance encourages timely information sharing with the board. It is noteworthy that in the theory of friendly boards (Adams and Ferreira, 2007), there is no presumption that a friendlier board would necessarily increase or decrease firm value. This follows because, to the extent that there is an interior optimum level of board independence, a friendlier board could affect firm value in either direction. Lee, Lee, and

Nagarajan (2014) find that more homophily lowers Tobin's Q. We confirm their findings and provide new evidence that while this negative relationship is observed for subsamples with weaker shareholder governance, there is no such association for the subsample of stronger shareholder governance.

## 1. Related Literature

Our paper relates to the literature on friendly boards. In the theoretical model proposed by Adams and Ferreira (2007), the CEO faces a trade-off when she decides whether or not to disclose private information to the board. If the CEO shares information with the board, she will be able to gain better advice. However, sharing private information imposes costs on the CEO, as a more informed board would monitor the CEO more intensively. Holmstrom (2005), Raheja (2005), and Harris and Raviv (2008) also provide models suggesting that the presence of independent directors may affect the advising role of the board.

Faleye, Hoitash, and Hoitash (2011) highlight the trade-offs between independent directors' monitoring and advising roles, and show that when a majority of independent directors sit on two or three important monitoring committees, the quality of monitoring improves at the expense of advising, and firm value deteriorates. The authors argue that when the board monitors more intensively, it receives less strategic information. Armstrong, Core, and Guay (2014) demonstrate that an increase in the proportion of independent directors leads to greater corporate transparency. This is because independent directors require a transparent information environment to effectively monitor and advise the management. In addition, Schmidt (2015) examines social connections between the CEO and board members and finds that for acquirer firms with severe agency problems, the social ties are associated with worse acquirer returns, suggesting weaker monitoring. Conversely, for acquirer firms where the board's advisory role is more important, the

social ties are associated with higher acquirer returns. Kang, Liu, Low, and Zhang (2018) also measure board friendliness using CEO-director social ties and find that firms with friendly boards tend to produce more patents and receive more citations, especially when firms' advisory needs are higher.

Our paper also relates to the literature on the political views of corporate stakeholders. For example, Hong and Kostovetsky (2012) find that Democratic-oriented mutual fund managers are less likely to invest in socially irresponsible firms.[6] Wintoki and Xi (2020) demonstrate that fund managers are more likely to allocate assets to firms whose executives and directors share the fund managers' partisan affiliations. Kempf and Tsoutsoura (2021) find that credit analysts tend to downgrade firms when the political party in power is not aligned with their own views. Finally, a recent paper by Arikan et al. (2022) reveals that the partisan alignment between CEOs and the U.S. president affects corporate disclosures. We add to this literature by showing that the partisan alignment between CEOs and independent directors facilitates the information sharing between them.

Finally, our paper extends the literature on accounting conservatism, which refers to the tendency for 'bad news' to be reflected more quickly than 'good news' in a firm's financial reporting (Basu, 1997; Lawrence, Sloan, and Sun, 2013). Managers may be incentivized to withhold bad news due to career concerns, hoping that future events will allow them to "bury" the bad news (Kothari, Shu, and Wysocki, 2009). Lara, Osma, and Penalva (2009) show that stronger corporate governance can limit the withholding of bad news and lead to greater accounting conservatism. Similarly, Ahmed and Duellman (2007) document that board independence is

[6] Hutton, Jiang, and Kumar (2014) show that Republican managers adopt more conservative corporate policies. Di Giuli and Kostovestky (2014) find that firms with Democratic executives spend more on corporate social responsibility.

positively associated with conservatism, while Goh and Li (2011) find that firms with weaker internal control quality exhibit less conservatism. In addition, Jayaraman (2012) shows that enforcement of insider trading laws increases firms' timely recognition of losses. Our paper builds on this literature by showing that a CEOs and boards who trust one another can reduce career concerns and encourage timely corrective actions.

## 2. Sample and Measure Constructions

### 2.1 Construction of the Political Homophily Index

We obtain the data on CEOs from the Execucomp database and the data on independent directors from BoardEx. Our baseline sample includes the firms that are covered by both the Execucomp and the BoardEx databases and have all the regression variables available. The sample consists of 26,228 firm-years between 1999 and 2019, and each firm-year has an average of 7.6 independent directors.

Following standard practice in the literature (e.g., Hong and Kostovetsky, 2012; Di Giuli and Kostovetsky, 2014; Hutton, Jiang, and Kumar, 2014, 2015; Lee, Lee, and Nagarajan, 2014), we collect the individual campaign donation data from the website of the Federal Election Commission (FEC) to measure the political leanings of the directors and CEOs. The FEC individual contributions file contains information about each contribution made by an individual to a political committee/candidate, which is disclosed by the recipient of the contribution under the requirement of federal law.[7] Our sample includes contributions made to candidate committees, party committees, as well as hybrid PACs and super PACs with partisan affiliations. The party

[7] Note that not all individual donations are subject to mandatory disclosure. In 1989-2014, a contribution was required to reported if the reporting period amount is $200 or more. After 2014, a contribution is required to be reported if the person's total donation to-date during the current election cycle is over $200 for a candidate or if the total calendar year-to-date donation is over $200 for political action committees (PACs) and party committees. We include only the donations subject to mandatory disclosure in the sample to avoid potential selection bias of voluntary disclosure.

affiliations of candidates and party committees are obtained from the committee master file provided by the FEC. For the hybrid PACs and super PACs which have more than 1,000 transaction records, we manually search for the political orientations of the PACs using OpenSecrets.org and Google.com. For each individual donation, we obtain the date of donation, the dollar amount, the employer of the donor, and the party affiliation of the recipient. We then match the donation records to the CEOs from Execucomp and directors from BoardEx by names and employers.

Following the literature (e.g., Hong and Kostovetsky, 2012; Hutton, Jiang, and Kumar, 2014, 2015), we first calculate each CEO/director's Republican index, *Rep*, using the following equation:

$$Rep_{p,t} = \frac{R_{p,t} - D_{p,t}}{R_{p,t} + D_{p,t}}, \quad (1)$$

where $R_{p,t}$ ($D_{p,t}$) denotes the total dollar amount of donations made by individual *p* to Republican (Democratic) recipients in the election cycle preceding year *t*. *Rep* therefore captures the time-varying political leaning of the CEOs and directors, with a higher value of *Rep* indicating that the individual is more Republican-oriented. We then calculate the CEO-board political homophily index, *PHI*, for each firm-year using the following equation:

$$PHI_{i,t} = 1 - \frac{|RepCEO_{i,t} - RepIndep_{i,t}|}{2}, \quad (2)$$

where $RepCEO_{i,t}$ is the Republican index of the CEO of firm *i* in year *t*. $RepIndep_{i,t}$ is the equal-weighted average Republican index of the independent directors of firm *i* in year *t*. By construction, *PHI* is bounded between zero and one. A higher *PHI* indicates that the CEO and independent directors of the firm are more politically aligned.

**2.2 Construction of the Crash Risk Measures**

We construct two measures for crash risk, namely, negative coefficient of skewness and down-to-up volatility, following the literature (e.g., Chen, Hong, and Stein, 2001; Xu, Xuan, and Zheng, 2021). We first estimate firm-specific daily returns for each firm-year using the following regression:

$$r_{i,d} = \alpha + \beta_1 r_{m,d-2} + \beta_2 r_{m,d-1} + \beta_3 r_{m,d} + \beta_4 r_{m,d+1} + \beta_5 r_{m,d+2} + \epsilon_{i,d}, \quad (3)$$

where $r_{i,d}$ is return of stock *i* on day *d*, and $r_{m,d}$ is return of the CRSP value-weighted market index on day *d*. The firm-specific daily returns, denoted by $R_{i,d}$, is calculated as the natural logarithm of one plus the residual return in Equation (3).

The first measure, negative coefficient of skewness (*NCSKEW*), is calculated for each firm-year as the opposite number of the third moment of the firm-specific daily returns divided by the standard deviation of the firm-specific daily returns raised to the third power:

$$NCSKEW_{i,t} = -\left[n(n-1)^{\frac{3}{2}} \sum R_{i,d}^3\right] / \left[(n-1)(n-2)(\sum R_{i,d}^2)^{\frac{3}{2}}\right], \quad (4)$$

The second measure, down-to-up volatility (*DUVOL*), is calculated as follows:

$$DUVOL_{i,t} = log\{\left[(n_u - 1) \sum_{DOWN} R_{i,d}^2\right] / \left[(n_d - 1) \sum_{UP} R_{i,d}^2\right]\}, \quad (5)$$

where "DOWN" ("UP") indicates the days when the firm-specific returns are below (above) the mean of year *t*. $n_u$ ($n_d$) is the number of up (down) days of firm *i* in year *t*. Higher values of these two measures indicate greater crash risks.

**2.3 Summary Statistics**

Table 1 presents the summary statistics of the variables used in our paper. The dependent variable, *NCSKEW*, has a mean of 0.04 and a standard deviation of 1.64. *DUVOL* has a mean of -0.03 and a standard deviation of 0.34. The average CEO Republican orientation (*RepCEO*) is 0.14, whereas the average independent director Republican orientation (*RepIndep*) is 0.03, indicating

that the CEOs are on average more Republican-orientated than the directors. The independent variable of interest, *PHI*, has a mean of 0.80 and a standard deviation of 0.21.

We also construct a number of firm characteristics as control variables following the prior literature (e.g., Chen, Hong, and Stein, 2001; Kim, Li, and Zhang, 2011a, 2011b; Callen and Fang, 2015; DeFond et al, 2015; Xu, Xuan, and Zheng, 2021; Hsu, Wang, and Whipple, 2022). These variables include firm-specific stock return volatility in year *t* (*Sigma*), the cumulative firm-specific daily returns in year *t* (*Ret*), the average monthly share turnover in year *t* minus the average monthly share turnover in year *t-1* (*Dturn*), market-to-book ratio (*MB*), book leverage (*Lev*), return on assets (*ROA*), the natural logarithm of market value (*LnMV*), and the absolute value of discretionary accruals (*DA*). We also control for the natural logarithm of board size (*LnBoardSize*) and the percentage of a firm's directors who are socially connected to the CEO (*Connection*). Following Dasgupta, Zhang, and Zhu (2015), we define a director as connected to a CEO if (1) the director and the CEO studied at the same institution during an overlapping period, or (2) they worked for the same firm (other than the focal firm) at least five years before they started working for the focal firm. Table 1 also presents the summary statistics of these control variables.

## 3. Empirical Results

### 3.1 Political Homophily and Crash Risk

As discussed in the previous section, if political homophily facilitates the CEO's sharing of negative private information with the board, then we expect political homophily to be associated with lower future crash risk. In this section, we test this hypothesis by first estimating the baseline panel regressions, and then using Sinclair acquisitions to address endogeneity.

#### *3.1.1 Panel Regressions of Crash Risk on Political Homophily*

To examine the relationship between crash risk and political homophily, we estimate the following panel regression:

$$Crash\_Risk_{i,t} = \alpha + \beta_1 PHI_{i,t-1} + \sum_k \beta_k Controls^k_{i,t-1} + \varphi_i + \eta_t + \epsilon_{i,t}, \quad (6)$$

where $Crash\_Risk_{i,t}$ is the crash risk of firm $i$ in year $t$, measured by negative coefficient of skewness ($NCSKEW_{i,t}$) or down-to-up volatility ($DUVOL_{i,t}$). $PHI_{i,t-1}$ is the political homophily index of firm $i$ in year $t-1$. $Controls_{i,t-1}$ is a set of firm-level control variables as discussed in the previous section. For the ease of interpretation, we standardize the crash risk measures ($NCSKEW_{i,t}$ and $DUVOL_{i,t}$) and the main independent variable of interest, $PHI_{i,t-1}$, to have means of zero and standard deviations of one. We include firm and year fixed effects in the regressions and cluster standard errors at the firm level.

Columns (1) and (2) of Table 2 report the regressions using $NCSKEW_{i,t}$ and $DUVOL_{i,t}$ as the dependent variables, respectively. As can be seen, the coefficient on $PHI_{i,t-1}$ is negative and statistically significant at the 1% level in both specifications. In terms of economic magnitude, the coefficient estimate implies that a one standard deviation increase in *PHI* is associated with a 2.3% standard deviation decrease in *NCSKEW* and a 2.5% standard deviation decrease in *DUVOL*. We stress the directional results rather than the economic magnitude because the latter depends not only on by how much political homophily affects information sharing but also the rate of arrival of adverse information and how acting on that information subsequently affects stock returns. Even when adverse information arrives infrequently, not talking timely actions on the basis of that information can have major consequences for shareholders. Taken together, the results presented in Table 2 indicate that, consistent with our prediction, political homophily is negatively associated with future stock price crash risk.

*3.1.2 Robustness Tests*

We follow Lee, Lee, and Nagarajan (2014) and conduct robustness checks using alternative measures of *PHI* based on different assumptions on individuals' political leanings. Specifically, *PHI (Time-invariant)* is the political homophily index constructed using the individuals' Republican index based on their total amount of contribution up to the year 2019 (rather than the previous political cycle).[8] The second alternative measure is *PHI (Prior)*. To construct this measure, we first calculate the Republican index for each individual *p* in year *t* using her historical contribution made before year *t*, and then aggregate it at the firm level. The third alternative measure, *PHI (Strong)*, is the political homophily index constructed using the Republican index of the individuals whose contribution to one party net of her contribution to the other party exceeds $2,000 in an election cycle. This measure is constructed following Hong and Kostovetsky (2012) to capture the political views of only those individuals who have strong partisanship. The fourth alternative measure, *PHI (Large)*, is the political homophily index constructed using the Republican index of the individuals whose historical total amount of contribution exceeds $2,000. This measure intends to reduce the noise induced by small donors.

We estimate a model similar to Equation (6) but using the four alternative *PHI* measures discussed above. The results are presented in Table 3, in which Panel A reports the regressions using *NCSKEW* (*DUVOL*) as the dependent variable and Panel B reports the regressions using *DUVOL* as the dependent variable. As can be seen, in all four sets of regressions, the negative association between *PHI* and future crash risk is robust when we use alternative measures of *PHI* (t-statistics ranging from -2.43 to -3.47).

Furthermore, one could argue that the baseline results may be driven by the relation between a firm's crash risk and the political orientation of its directors, rather than that the relation

[8] This time-invariant measure of *PHI* can reduce the measurement error of political orientation in election cycles, but potentially has forward-looking bias.

between crash risk and political homophily between the CEO and directors. To investigate this possibility, we perform similar regressions to those specified by Equation (6), including *RepIndep*, the average Republican index of a firm's directors, as an additional control variable. As reported in Panel C of Table 3, the inclusion of *RepIndep* as a control variable does not alter the economic or statistical significance of the coefficient on *PHI*. In addition, the coefficients on *RepIndep* are not statistically significant. Hence, our baseline results are unlikely to be driven by the relation between a firm's crash risk and the political orientation of its directors.

*3.1.2 Identification Using Sinclair Acquisitions*

We acknowledge that the observed negative relation between *PHI* and crash risk can be caused by omitted variables, especially because the appointment decisions of CEO or directors are not exogenous. For example, some omitted firm characteristics may attract CEOs and independent directors with aligned political views and these same characteristics could be associated with policies that reduce crash risk. Therefore, to identify the causal effect of political homophily on crash risk, we exploit the exogenous variations in the independent directors' political views caused by Sinclair Broadcast Group's acquisitions of local television stations.

Our approach is motivated by the existing literature that people's political views can be significantly affected by public media programs and propaganda (e,g, DellaVigna and Kaplan, 2007; Durante, Pinotti, and Tesei, 2019). Recent studies also find that access to broadband internet and more media choices contribute to the increased political polarization in the past decades (e.g., Prior, 2007; Lelkes, Sood, and Iyengar, 2017).

Sinclair began its rapid expansion in the United States in the early 1980s by acquiring local television stations across the states. In the year 2019, Sinclair was the largest local television station operator in the U.S. in terms of both the number of stations owned (191) and the coverage

(89% of U.S. markets).[9] The company is documented by both media and academic researchers to have strong Republican-leaning views (e.g., Glaser, 2018; Martin and McCrain, 2019), as it often broadcasts news that is in favor of the Republicans. A recent study by Ren (2020) finds that the acquisitions of local TV stations by Sinclair significantly shifts local residents' political orientation towards Republican. Ren (2020) further shows that the Sinclair acquisitions are unlikely to be driven by local economic condition or political leaning, and therefore unlikely to be related to fundamentals of firms. Therefore, we exploit the exogenous shock caused by the Sinclair acquisitions to people's political orientation and in turn political homophily.

We obtain information on Sinclair's acquisitions of local TV stations from RabbitEars.info, which is a database that contains comprehensive information on media markets in the U.S. The sample consists of 163 acquisitions made by Sinclair in 96 designated market areas (DMA) from 1984 to 2018. To identify the location of a CEO or director, we take the self-disclosed addresses in her FEC donation records and use the county in which she makes the largest amount of donation in a given year as her county of residence in that year. In the cases where a CEO or director's address cannot be found in the FEC database, we use her firm's headquarter county as her county of residence.[10] We then match the CEOs and directors' counties of residence to DMAs using the DMA-county matching information from Wikipedia.[11]

To examine whether the Sinclair acquisitions significantly affect the political orientation of independent directors and CEOs, we estimate the following OLS regression:

[9] For details, see the official Sinclair website at http://sbgi.net/.

[10] Since firms may change their headquarters locations (e.g., Heider and Ljungqvist, 2015), we obtain the firms' historical headquarter addresses by scraping the firms' index pages on the Electronic Data Gathering, Analysis, and Retrieval system (EDGAR). If a director works for multiple companies in the same year, then we use the headquarters county of the firm in which the director holds an executive position as her county of residence. In the few cases where a director holds executive positions in multiple companies, or does not hold an executive position, we use the headquarters county of the firm for which she has worked for the longest period as her county of residence.

[11] The information can be found at https://en.wikipedia.org/wiki/List_of_United_States_television_markets.

$$REP_{p,t} = \alpha + \beta_1 Sinclair_{p,t-1} + \sum_k \beta_k Controls^k_{p,j,t-1} + \epsilon_{i,t}, \quad (7)$$

where $REP_{i,t}$ is the Republican index of director or CEO $p$ in year $t$, and $Sinclair_{i,t-1}$ is a dummy variable that equals one if the director or CEO is affected by a Sinclair acquisition in her county of residence in year *t-1*, and zero otherwise. We include the same set of firm-level control variables ($Controls_{p,j,t-1}$) as those in Equation (6). If a director holds positions in multiple firms within a year, the firm characteristics are obtained from the company where the director has held the position for the longest duration. We also include firm fixed effects and year fixed effects in the regressions.

Column (1) of Table 4 presents the regression for our sample directors, which shows that the Sinclair acquisitions significantly shift the directors' political leaning towards Republican. Specifically, the coefficient of Sinclair is positive and significant at the 1% level. This effect is also economically significant, as the coefficient indicates that a Sinclair acquisition increases a director's *REP* by 0.020, which is approximately 64.5% of its sample mean (=0.020/0.031). Column (2) presents the regression for sample CEOs, which shows that, interestingly, the Sinclair acquisitions do not have a significant impact on CEOs' political leaning. This is possibly due to two reasons. First, as noted earlier, the CEOs are ex-ante much more Republican-oriented than the directors and therefore the marginal effect of Sinclair broadcast acquisitions may be lower for CEOs. Second, it has been well documented that CEOs are more likely to be overconfident (e.g., Malmendier and Tate, 2005, 2008), which may also make CEOs update their political views to a lesser degree than directors in response to media. These findings are consistent with Ren (2020) who finds that Sinclair acquisitions significantly shift non-CEO employees' political contributions towards Republicans but do not affect the CEOs' contributions.

*3.1.3 Sinclair-predicted PHI and Crash Risk*

The previous sub-section shows that Sinclair acquisitions have a significant impact on the political orientations of directors, which in turn can affect the CEO-board political homophily. This validates the Sinclair acquisitions as a valid instrument for *PHI*. Consequently, we adopt a three-stage approach following Adams, Almeida, and Ferreira (2009) to determine the causal impact of *PHI* on firms' crash risk. Specifically, in the first stage, we estimate the model specified by Equation (7). In the second stage, we compute the political homophily index using individual directors' Republican indices predicted in the first stage (*PHISinclair*).[12] In the third stage, we utilize *PHISinclair* as the instrument for *PHI* and apply an instrumental variable approach to estimate Equation (6).

The results of the third stage of the procedure are presented in Table 5, which shows that the coefficients on *PHI* are similar to those in our baseline regressions (-0.024 for both *NCSKEW* and *DUVOL*) and are statistically significant at the 1% level (t-statistics -2.92 for *NCSKEW* and -3.01 for *DUVOL*). These findings indicate that the exogenous variation in political homophily brought about by the Sinclair acquisitions have a significant impact on firms' future crash risk. For the remaining empirical tests in the paper, we will utilize the three-step procedure when *PHI* is included as an independent variable.[13]

### 3.2 Mechanisms of the Effect of Board Friendliness on Crash Risk

Our results so far have shown that political homophily has a significantly negative impact on future crash risk. We hypothesize that *PHI* negatively affects crash risk by encouraging the CEOs to share negative information with the board members, therefore allowing them to take

[12] Since Table 4 demonstrates that the Sinclair acquisitions do not significantly affect the political views of CEOs, we construct *PHISinclair* using the predicted Republican index for directors and the raw Republican index for CEOs.
[13] Note that the first and second steps of the procedure are always executed using the model specified by Equation (7). The specifications of the third step may vary depending on the models specified for the particular tests to be discussed in the following sections.

actions and prevent potentially adverse events from actually happening. Although we cannot directly observe the communication between the CEOs and directors, we conduct two tests to provide supporting evidence on the mechanism of information sharing. Specifically, we examine if political homophily increases the directors' insider trading returns, and if political homophily increases the firms' likelihood to sell off previously acquired assets with poor acquisition announcement returns, and write down assets with depreciated value.

*3.2.1 Board Friendliness, Information Sharing, and Insider Trading Returns*

It is well documented that corporate insiders use their private information about the firms to earn excess returns from insider trading (see, e.g., Bushman and Indjejikian, 1995). Ravina and Sapienza (2010) find that independent directors earn significantly positive returns on their insider purchases, but their performance is lower than that of executives. This finding supports the notion that executives possess more private information about their firms than independent directors. If political homophily encourages CEOs to share private information with the directors, then increased information sharing could boost independent directors' insider trading returns and narrow their performance gaps with executives.

We examine this conjecture by obtaining insider purchases made by directors and executives from Thomson Reuter's Insider Data for our sample firms.[14] Following Ravina and Sapienza (2010), we calculate the market-adjusted returns of an individual's long position for 0, 30, 60, 90, and 180 trading days. For each insider, we assign a dummy variable (*Independent*) that equals one if the person is an independent director, and zero otherwise. As argued in Fidrmuc, Goergen, and Renneboog (2006), transaction size could potentially correlate with informativeness of the insider trading. We therefore calculate the trade size for each transaction as a fraction of the

[14] We focus on insider purchases rather than sales since Ravina and Sapienza (2010) argue that purchases are more likely to be information-driven.

firm's market capitalization (*TradeSize*). We then regress insider trading returns on the triple interaction among *PHI*, *Independent*, and *TradeSize*.[15] Other control variables include return on assets (*ROA*), the ratio of capital expenditure to property, plant, and equipment (*CAPEX*), the ratio of R&D expenses to total assets (*RD*, set to zero is missing), the natural logarithm of total assets (*LnAsset*), book leverage (*Lev*), the natural logarithm of board size (*LnBoardSize*), and the percentage of board members connected to the CEO (*Connection*). For ease of interpretation, we standardize the insider trading return variables and *PHI* to have means of zero and standard deviations of one.

Table 6 reports the results, in which Columns (1) to (5) present regressions for various return windows from one day to 180 days. The interaction between *PHI*, *Independent*, and *TradeSize* is significantly positive in all specifications except one-day returns, indicating that the insider trades made by independent directors in firms with higher *PHI* are more profitable. The coefficients on *TradeSize* are significantly positive and the coefficients on the interaction between *Independent* and *TradeSize* are significantly negative, which is consistent with Ravina and Sapienza (2010) who find that larger trades made by insiders are more informative and that independent directors have less private information than executives do. These results support the hypothesis that higher *PHI* encourages the CEO to share more information with the independent directors.

*3.2.2 Board Friendliness and the Subsequent Divestitures of Acquired Assets*

In this subsection, we examine whether a friendly board (a board with high *PHI*) makes the CEO more willing to admit her mistakes in decision-making. Specifically, we identify the CEOs' willingness to admit their mistakes by testing whether the firms will sell off previously

[15] The interaction terms involving PHI are instrumented by the interaction terms between PHISinclair and the other two variables.

acquired assets that are perceived to have lower value. We obtain the sample of completed acquisitions from the Capital IQ Mergers and Acquisitions Database, and then identify, for each acquisition, whether the acquired firm is subsequently sold off by the acquirer.[16] To measure the perceived value of an acquisition to the acquirer, we calculate the acquirer's cumulative abnormal return (CAR), estimated using the market model, in the three trading days centered on the original acquisition announcement date. We then estimate the following linear probability model:

$$Divest_j = \alpha + \beta_1 PHI_j \times CAR_j + \beta_2 PHI_j + \beta_3 CAR_j + \sum_k \beta_k Controls_j^k + \eta_t + \epsilon_j, \quad (9)$$

where $Divest_j$ is a dummy variable that equals one if the acquired firm in transaction $j$ is subsequently divested in the three years after the completion date of the acquisition. The variable of interest is the interaction between $PHI_j$ and the acquirer's three-day CAR around the announcement date of transaction $j$ ($CAR_j$). *PHI* and its interaction with *CAR* are instrumented by *PHISinclair* and its interaction with *CAR*. $Controls_j$ is a vector of control variables that include the natural logarithm of the acquirer's total assets ($AcqSize_j$), the acquirer's market-to-book ratio ($AcqMB_j$), the acquirer's book leverage ($AcqLev_j$), the acquirer's return on assets ($AcqROA_j$), the natural logarithm of the value of the acquisition ($LnDealValue_j$, set to zero if missing), a dummy variable that equals one if the transaction value is missing, and zero otherwise ($MissingDealValue_j$), a hostile takeover dummy ($Hostile_j$), a stock merger dummy ($Stock_j$), and a tender offer dummy ($Tender_j$).[17] The acquirer variables are measured at the end of the fiscal year before the merger announcement date. We also include year fixed effects in the regressions. To

[16] Since Capital IQ uses a unique identifier (FIRMID) to track each firm even after it is acquired, we are able to identify the acquired firms that are subsequently sold off.

[17] Since most of the sample acquisitions have private targets, we are unable to control for target characteristics which are available for only a small portion of the sample. Therefore, we control for a broad set of acquirer characteristics and deal characteristics available in Capital IQ.

facilitate interpretation, we standardize *PHI* to have a mean of zero and a standard deviation of one.

Column (1) of Table 7 presents the regression of $Divest_j$ on $CAR_j$, in which the coefficient on $CAR_j$ is significantly negative (t-statistic -2.47). This result indicates that the acquired assets with lower perceived values to the acquirers are more likely to be divested in the future. Column (2) presents the regression of $Divest_j$ on the interaction between $PHI_j$ and $CAR_j$. The interaction is negative and significant at the 5% level (t-statistic -2.46), suggesting that acquirers with greater political homophily are more likely to divest lower-valued acquired assets. We further include industry fixed effects (at the two-digit SIC level) into the regressions and report the results in Columns (3) and (4). The coefficient on the interaction between $PHI_j$ and $CAR_j$ remains significant in this specification (t-statistics -2.24). Taken together, the results in Table 7 suggest that political homophily makes CEOs more willing to admit their mistakes and in turn sell off acquired assets with low value.

*3.2.3 Board Friendliness and Asset Write-Downs*

In this subsection, we examine the relation between board friendliness and accounting conservatism, specifically, if political homophily affects firms' decisions on asset write-downs. On the one hand, Lawrence, Sloan, and Sun (2013) document that firms with higher book-to-market ratios have larger asset write-downs, which is consistent with the accounting rules under Generally Accepted Accounting Principles (GAAP) that require assets to be written down when their fair values drop sufficiently below book values. On the other hand, the subjectivity in GAAP, such as the flexibility in determining the face value of goodwill, enables managers to exercise discretions on write-downs. We therefore hypothesize that a friendly board incentivizes the CEO to recognize losses in asset value, which leads to larger assets write-downs.

We follow Lawrence, Sloan, and Sun (2013) and construct two measures of asset write-downs. The first measure, *SPI*, is defined as a firm's special items scaled by its market capitalization at the end of previous year. The second measure, $WD_t$, is defined as the sum of the firm's asset write-downs and goodwill impairments, scaled by its market capitalization at the end of previous year.[18] As a starting point, we first estimate an OLS regression where the dependent variable is one of the two write-down measures in year *t*, and the independent variable is $BTM_{t-1}$, defined as the firm's book-to-market ratio in year *t-1*. For ease of interpretation, we standardize the asset write-down measures and BTM to have means of zero and standard deviations of one. We also include firm and year fixed effects in the regressions. Columns (1) and (3) of Table 8 present the regression results. We find a significantly negative coefficient of book-to-market ratio in both regressions. Since write-downs are recorded in negative values, the negative coefficients indicate that, consistent with Lawrence, Sloan, and Sun (2013), higher book-to-market firms have larger asset write-downs.

Next, we include the interaction between *PHI* and book-to-market ratio in the regressions, as well as the firm-level control variables.[19] As shown in Columns (2) and (4) of Table 8, the coefficient of the interaction term is significantly negative in both regressions (t-statistics -2.01 and -1.77). Since write-downs are recorded in negative values, these negative coefficients suggest that among high book-to-market firms where assets write-downs are expected, firms with higher political homophily are more likely recognize losses in asset value.[20] Overall, the results in Table

[18] Special items include significant nonrecurring items, asset write-downs, impairments of goodwill, and restructuring charges.

[19] We also standardize *PHI* for ease of interpretation. *PHI* and its interaction with book-to-market ratio are instrumented by *PHISinclair* and its interaction with book-to-market ratio.

[20] We conduct an untabulated analysis where we regress asset write-down measures on *PHI* and controls (without the interaction term) and find that the coefficient on *PHI* is insignificant, which indicates that the effect of board friendliness on write-downs is concentrated in high book-to-market firms.

8 are consistent with our hypothesis that friendly board encourages managers to recognize previously made mistakes.

*3.2.4 Alternative Explanation Based on Risk Taking*

Our previous findings suggest that the lower crash risk associated with political homophily is a manifestation of better information sharing and more timely actions. However, it is worth noting that lower crash risk could also be caused by less risk taking. Specifically, if political homophily helps CEO resist shareholder pressure for pursuing risky strategies, then we will also observe a negative association between *PHI* and crash risk but the channel is a lower level of general risk-taking rather than better information sharing.[21] To examine this alternative explanation, we examine the relation between a firm's political homophily and the firm's risk-taking. Specifically, we estimate the following model:

$$RiskTaking_{i,t} = \alpha + \beta_1 PHI_{i,t-1} + \sum_k \beta_k Controls^k_{i,t-1} + \varphi_i + \eta_t + \epsilon_i, \quad (10)$$

where *RiskTaking* is one of the three measures of risk taking, including book leverage ($Lev_t$), stock return volatility ($Vol_t$), and idiosyncratic return volatility ($IdioVol_t$, estimated using the Fama-French three-factor model). *PHI* is instrumented by *PHISinclair*. $Controls_{i,t-1}$ is a vector of control variables which include return on assets ($ROA_{i,t-1}$), the ratio of capital expenditure to property, plant, and equipment ($CAPEX_{i,t-1}$), the ratio of R&D expenses to total assets ($RD_{i,t-1}$, set to zero is missing), the natural logarithm of total assets ($LnAsset_{i,t-1}$), lagged book leverage ($Lev_{i,t-1}$), the natural logarithm of board size ($LnBoardSize_{i,t-1}$), and the percentage of board members connected to the CEO ($Connection_{i,t-1}$). For ease of interpretation, we standardize the risk taking measures

[21] Giannetti and Zhao (2019) find that discrepancy in board members' opinions and values may lead to inefficiencies in the decision-making process and performance volatility. It is also possible that political homophily reduces the conflicts and uncertainties in decision-making, so *PHI* negatively associates with general performance volatility.

and *PHI* to have means of zero and standard deviations of one. We also include firm and year fixed effects in the regressions.

Table 9 presents the regression results. We find that the coefficient of *PHISinclair* is positive (rather than negative) and insignificant in each regression (t-statistics from -0.08 to 0.30), which suggests that greater political homophily does not lead to lower level of risk taking. These results show that the negative impact of political homophily on crash risk is unlikely a reflection of less risk-taking by firms with greater political homophily.

## 4. Corporate Governance and the Effect of Political Homophily

In previous sections we have shown that the political alignment between CEOs and directors decreases future crash risk. We argue that the channel through which this comes about is that friendly boards encourage the CEO to share information, especially negative information. The motivation for negative information sharing is a tradeoff for CEOs. On the one hand, past poor decisions may reflect poorly on the CEO, which can lead to a penalty to the CEO for such decisions. On the other hand, such disclosures make it possible to take more timely corrective actions so that worse future outcomes are avoided. A friendly board is likely to penalize the CEO less for such decisions, which encourages negative information sharing by the CEO. On the contrary, if the board is not friendly, the CEO might prefer not to disclose negative information and instead take a chance that the problem will get resolved, or might even look for alternative employment before the problem manifests.

However, this argument presupposes that a friendly board would not be able to stand by the CEO if the CEO does not take immediate corrective action and in turn causes a publicly

observable negative outcome. If the CEO gets "downside protection" from a friendly board, she might prefer not to disclose ex ante negative information because disclosure of such information could come at some immediate costs to the CEO, such as the board (even when friendly) tying the CEOs hands, or divesting pet projects. Therefore, if the CEO has downside protection from the friendly board, she might try to avoid such costs and take a chance that the problem will get resolved.

Thus, whether or not a friendly board encourages negative information sharing depends on the extent of this downside protection. This is where corporate governance, and in particular, shareholder power, is important. We argue that a friendly board would not be able to offer downside protection when shareholder power is high. This implies that the observed negative relation between political homophily and lower crash risk should only manifest when shareholder power is high. In our subsequent analysis, we use two common measures of shareholder power to test this implication: institutional ownership (e.g., Denis, Denis, and Sarin, 1997; Harford, Jenter, and Li, 2011) and the E-Index (e.g., Bebchuk, Ferrell, and Cohen, 2009). We first examine the negative relationship between *PHI* and crash risk for the subsamples of shareholder power. We then show that, consistent with our hypothesis, the CEO receives more protection from poor performance when the board is friendly, but only among firms with weak shareholder power. Finally, we examine how the relation between *PHI* and firm value varies across shareholder power.

*4.1 Board Friendliness, Governance, and Crash Risk*

We first examine if the negative relationship between *PHI* and crash risk only holds for firms with strong shareholder power. Panel A of Table 10 reports regressions of crash risk on *PHI* (instrumented by *PHISinclair*) for the two subsamples based on whether the firms' institutional ownership is above or below the sample median. The independent variable is *NCSKEW* in

Columns (1) and (2) and *DUVOL* in Columns (3) and (4). For ease of interpretation, we standardize the crash risk variables and *PHI* to have means of zero and standard deviations of one. As can be seen, the association between *PHI* and future crash risk is significantly negative in the high institutional-ownership subsample (t-statistics -2.71 and -3.17) but insignificant in the low institutional-ownership subsample (t-statistics -1.45 and -1.13).

In Panel B, we further present the regressions for the two subsamples based on E-index. We find that the coefficient of *PHI* is significantly negative in the low E-index subsample, but small and insignificant for the high E-index subsample. Therefore, the results using both corporate governance measures show that, consistent with our prediction, the association between *PHI* and future crash risk is significantly negative only for the firms with strong shareholder power.

*4.2 Board Friendliness, Governance, and CEO Turnover-performance Sensitivity*

In this subsection, we examine the relationship between political homophily and CEO turnover-performance sensitivity. As discussed earlier, we hypothesize that political homophily provides "downside protection" for CEOs only when shareholder power is weak. We test this hypothesis by estimate the following linear probability model:

$$Turnover_{i,t} = \alpha + \beta_1 PHI_{i,t-1} \times Ret_{i,(t-1,t-4)} + \beta_2 PHI_{i,t-1} + \beta_3 Ret_{i,(t-1,t-4)} + \sum_k \beta_k Controls^k_{i,t-1} + \varphi_i + \eta_t + \epsilon_i, \quad (11)$$

where $Turnover_{i,t}$ is a dummy variable that equals one if firm *i* experiences a CEO turnover in year *t*, and zero otherwise. Following Lee, Lee, and Nagarajan (2014), we use four-year cumulative stock return from year *t-4* to *t-1* as the measure of CEO performance. The variable of interest is the interaction between $PHI_{i,t-1}$ and $Ret_{i,(t-1,t-4)}$. *PHI* and its interaction with *Ret* are instrumented by *PHISinclair* and its interaction with *Ret*. $Controls_{i,t-1}$ is a vector of control variables including a dummy variable for CEO above 65-year-old ($RetireAge_{i,t-1}$), the natural logarithm of the CEO's

tenure ($LnTenure_{i,t-1}$), the natural logarithm of the firm's total assets ($LnAsset_{i,t-1}$), market to book ratio ($MB_{i,t-1}$), and a dummy variable for dividend-paying firms ($DividendPay_{i,t-1}$). For ease of interpretation, we standardize *PHI* to have a mean of zero and a standard deviation of one. We include firm and year fixed effects in the regressions.

Table 11 presents the regression results. Column (1) presents the regression of CEO turnover on past performance, in which the coefficient on *Ret* is significantly negative. This result indicates that CEOs with poor past performance are more likely to be replaced, which is consistent with the existing literature (e.g., Jenter and Lewellen, 2021). Column (2) further includes the interaction between *PHI* and *Ret.* We find that, consistent with Lee, Lee, and Nagarajan (2014), the coefficient of this interaction is significantly positive, indicating that CEO turnover-performance sensitivity is lower in firms with greater political homophily.

We then run the regressions separately for the subsamples based on corporate governance. Columns (3) and (5) show that the coefficient on *Ret* is significantly negative in both the subsamples with high and low institutional ownership. Columns (4) and (6) show that the interaction term between *PHI* and *Ret* becomes small and insignificant for high institutional-ownership firms but remains significantly positive for low institutional-ownership firms. This contrast shows that for firms with strong shareholder power, political homophily does not provide any downside protection for CEOs. We then turn to the subsamples based on the firms' E-index. Columns (7) and (9) show that the coefficient on *Ret* is negatively correlated with CEO turnover in both the subsamples with high and low E-index, with the coefficient in the subsample with low E-index being significant at the 1% level. Columns (8) and (10) show that the interaction between *PHISinclair* and *Ret* is insignificant for low E-index firms but remains significant for high E-index

firms.[22] Taken together, these results indicate that strong shareholder power seems a necessary condition for political homophily to encourage the CEO to share negative information with the board rather than hide it and in turn cause worse performance.

*4.3 Board Friendliness, Governance, and Firm Value*

Lee, Lee, and Nagarajan (2014) show that political homophily has a negative impact on firm value by reducing monitoring intensity. While our focus is the CEO's sharing of negative information, our results in the previous sections show that corporate governance interacts with the effect of political homophily. Therefore, in this subsection, we reexamine the relationship between political homophily, corporate governance, and firm value. Specifically, following Lee, Lee, and Nagarajan (2014), we estimate the following model:

$$Tobin's\ Q_{i,t} = \alpha + \beta_1 PHI_{i,t-1} + \sum_k \beta_k Controls^k_{i,t-1} + \varphi_i + \eta_t + \epsilon_i, \qquad (12)$$

where the specifications are similar to those in Equation (10), except that we replace the risk-taking measures with firms' Tobin's Q. For ease of interpretation, we standardize *Tobin's Q* and *PHI* to have means of zero and standard deviations of one. We also include firm and year fixed effects in the regressions.

Column (1) of Table 12 reports the regression results for the full sample. We find that the coefficient on *PHI* is significantly negative, indicating that, consistent with Lee, Lee, and Nagarajan (2014), political homophily negatively affects firm value. We then conduct the regression analysis separately for subsamples based on the corporate governance measures. Columns (2) and (3) present results for subsamples based on shareholder power, and Columns (4) and (5) present the results for subsamples based on E-index. We find that the coefficient on *PHI* is significantly negative only in the subsample of firms with low institutional ownership and the

[22] The coefficients on *Ret* in the subsamples with the inclusion of the interaction terms remain qualitatively similar to those without the inclusion of the interaction terms, although they are less statistically significant.

subsample of firms with high E-index. These results suggest that while political homophily leads to lower firm value, this effect is concentrated among firms with weaker shareholder power. For firms with strong shareholder power, political homophily does not lead to lower firm value, which suggests that for these firms, the negative effect of political homophily is potentially offset by the positive effect of better information sharing (and in turn more timely actions) when the CEO does not enjoy downside protection from a friendly board.

## 5. Conclusion

An influential idea in corporate governance is that a board that is predisposed to monitoring the CEO intensively (e.g., via committees without insider representation) may discourage the CEO from sharing information, which in turn may compromise the board's advisory role. There is some empirical evidence consistent with the broad concept that board "friendliness", as reflected, for example, by social connections between the CEO and independent board members, can both exacerbate agency problems as well as benefit the firm in situations where board expertise could be valuable. However, the crucial issue of whether friendliness encourages more information sharing has been difficult to establish.

In this paper, we argue that the similarity of political views promotes trust and bonding, and when the CEO and board enjoy greater political homophily, the CEO is encouraged to share adverse information with the board in a timely manner. We construct a measure of political homophily between the CEO and the board (the Political Homophily Index, *PHI*) using an individual's political donations. We find that firms' stock price crash risk decreases in *PHI*, which suggests that future negative outcomes are prevented via timely information sharing and the prompt addressing of problems. The results are robust when we instrument the *PHI* using

acquisitions of local television stations by the Sinclair Broadcast Group, known for its strong Republican-leaning views.

As evidence of information sharing, we show that insider trading profits are higher for independent directors when *PHI* is higher, suggesting that the directors do receive more information from the CEO. As evidence of corrective actions, we find that when *PHI* is higher, the firm is more likely to divest previously acquired assets that exhibited low performance, and to write down assets with depreciated value. Finally, we show that stronger shareholder governance is a necessary condition for the positive effect of a friendly board on information sharing: the effect of *PHI* on crash risks is only significant in firms with stronger shareholder rights (higher institutional ownership or lower E-index). Correspondingly, we find that higher *PHI* leads to lower CEO turnover-performance sensitivity, which is consistent with the "downside protection" provided by friendly boards, but such downside protection is absent in the subsample of strong shareholder governance. These results are consistent with the view that it is in the CEO's interest to share adverse information with a friendly board and to address problems in a timely manner when she may not enjoy "downside protection". Finally, we find that while for firms with weaker shareholder rights increases in *PHI* are associated with lower firm value, there is no effect of *PHI* on firm value in firms with strong shareholder governance, suggesting that the benefits of information sharing associated with friendly board can offset the costs of weak monitoring.

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**Table 1: Summary Statistics**

This table presents the summary statistics of the baseline sample. The sample consists of 26,228 firm-years covered by both Execucomp and BoardEx between 1999 and 2019. *NCSKEW* and *DUVOL* are two main measures of crash risk used in the paper. *NCSKEW* is the negative ratio of the third moment of firm-specific daily returns over the standard deviation of firm-specific daily returns raised to the third power. *DUVOL* is the natural logarithm of the ratio of down-day to up-day standard deviation of firm-specific returns. *PHI* is the political homophily index between a firm's CEO and independent directors. *PHISinclair* is the political homophily index calculated using directors' Republican indices predicted by Sinclair acquisitions. *RepCEO* is the Republican index of a firm's CEO. *RepIndep* is the average Republican index of a firm's independent directors. The other variables include firm-specific stock return volatility (*Sigma*), the cumulative firm-specific daily returns (*Ret*), the average monthly share turnover in year *t* minus the average monthly share turnover in year *t-1* (*Dturn*), market-to-book ratio (*MB*), book leverage (*Lev*), return on assets (*ROA*), the natural logarithm of market value (*LnMV*), the absolute value of discretionary accruals (*DA*), the natural logarithm of board size (*LnBoardSize*), and the percentage of a firm's directors who are socially connected to the CEO (*Connection*). Definitions of all other variables are provided in the Appendix.

| | Mean | Std | Q1 | Median | Q3 | N |
|---|---|---|---|---|---|---|
| Variable | (1) | (2) | (3) | (4) | (5) | (6) |
| *NCSKEW* | 0.040 | 1.636 | -0.621 | -0.064 | 0.565 | 26,228 |
| *DUVOL* | -0.026 | 0.343 | -0.230 | -0.037 | 0.168 | 26,228 |
| *PHI* | 0.795 | 0.210 | 0.563 | 0.910 | 1.000 | 26,228 |
| *PHISinclair* | 0.800 | 0.216 | 0.533 | 0.955 | 0.989 | 26,228 |
| *RepCEO* | 0.139 | 0.583 | 0.000 | 0.000 | 0.663 | 26,228 |
| *RepIndep* | 0.031 | 0.127 | 0.000 | 0.000 | 0.111 | 26,228 |
| *Sigma* | 0.022 | 0.012 | 0.013 | 0.019 | 0.026 | 26,228 |
| *Ret* | -0.049 | 0.332 | -0.247 | -0.088 | 0.094 | 26,228 |
| *Dturn* | 0.029 | 0.872 | -0.310 | 0.021 | 0.349 | 26,228 |
| *MB* | 2.982 | 3.906 | 1.388 | 2.155 | 3.594 | 26,228 |
| *Lev* | 0.187 | 0.176 | 0.024 | 0.157 | 0.293 | 26,228 |
| *ROA* | 0.120 | 0.097 | 0.068 | 0.117 | 0.171 | 26,228 |
| *LnMV* | 14.610 | 1.657 | 13.515 | 14.503 | 15.642 | 26,228 |
| *DA* | 0.156 | 0.387 | 0.024 | 0.054 | 0.113 | 26,228 |
| *LnBoardSize* | 2.033 | 0.310 | 1.792 | 2.079 | 2.303 | 26,228 |
| *Connection* | 0.024 | 0.073 | 0.000 | 0.000 | 0.000 | 26,228 |

**Table 2: Regressions of Crash Risk on Political Homophily**

This table presents the regressions of the crash risk measures on the political homophily index. *NCSKEW* is the negative ratio of the third moment of firm-specific daily returns over the standard deviation of firm-specific daily returns raised to the third power. *DUVOL* is the natural logarithm of the ratio of down-day to up-day standard deviation of firm-specific returns. *PHI* is the political homophily index between a firm's CEO and independent directors. Definitions of all other variables are provided in the Appendix. All regressions include firm and year fixed effects. Robust t-statistics, clustered by firm, are reported in parentheses. *, **, and *** represent statistical significance at the 10%, 5%, and 1% levels, respectively.

| Dep. Var. | $NCSKEW_t$ | $DUVOL_t$ |
|---|---|---|
| | (1) | (2) |
| $PHI_{t-1}$ | -0.023*** | -0.025*** |
| | (-2.96) | (-3.09) |
| $Sigma_{t-1}$ | 8.845*** | 4.978*** |
| | (6.96) | (4.41) |
| $Ret_{t-1}$ | 0.240*** | 0.300*** |
| | (12.40) | (15.45) |
| $Dturn_{t-1}$ | -0.002 | -0.003 |
| | (-0.22) | (-0.40) |
| $MB_{t-1}$ | 0.011*** | 0.012*** |
| | (5.37) | (5.71) |
| $Lev_{t-1}$ | -0.224*** | -0.264*** |
| | (-2.98) | (-3.41) |
| $ROA_{t-1}$ | 1.803*** | 2.143*** |
| | (13.45) | (15.64) |
| $LnMV_{t-1}$ | -0.254*** | -0.289*** |
| | (-15.52) | (-17.26) |
| $DA_{t-1}$ | 0.021 | 0.015 |
| | (1.08) | (0.82) |
| $LnBoardSize_{t-1}$ | 0.200*** | 0.215*** |
| | (4.55) | (4.79) |
| $Connection_{t-1}$ | -0.138 | -0.082 |
| | (-0.97) | (-0.56) |
| Firm FE | Yes | Yes |
| Year FE | Yes | Yes |
| Observations | 26,228 | 26,228 |
| $R^2$ | 0.152 | 0.165 |

**Table 3: Robustness Tests**

This table presents the robustness tests on the relation between *PHI* and crash risk. Panels A and B report the regressions of crash risk measures on the alternative measures of political homophily. *PHI (Individual)* is the alternative political homophily index constructed using the individuals' time-invariant Republican index calculated using their cumulative amounts of contributions up to the year 2019. *PHI (Prior)* is the alternative political homophily index constructed using the individuals' historic Republican index (i.e., for each individual *p* in year *t*, the Republican index calculated using her historic contribution made before year *t*). *PHI (Strong)* is the alternative political homophily index constructed using the Republican index of the individuals whose differences in contributions to the two parties exceed $2,000 in the election cycle. *PHI (Large)* is the alternative political homophily index constructed using the Republican index of the individuals whose historical total amounts of contribution exceed $2,000. Control variables are included but not reported to conserve space. Panel C reports the baseline regressions including *RepIndep*, the average Republican index of a firm's directors, as an additional control variable. All regressions include firm and year fixed effects. Robust t-statistics, clustered by firm, are reported in parentheses. *, **, and *** represent statistical significance at the 10%, 5%, and 1% levels, respectively.

**Panel A: Regressions of Negative Coefficient of Skewness on Alternative PHI Measures**

| Dep. Var. | $NCSKEW_t$ | | | |
|---|---|---|---|---|
| | (1) | (2) | (3) | (4) |
| $PHI_{t-1}$ *(Time-invariant)* | -0.025** | | | |
| | (-2.43) | | | |
| $PHI_{t-1}$ *(Prior)* | | -0.035*** | | |
| | | (-3.17) | | |
| $PHI_{t-1}$ *(Strong)* | | | -0.030*** | |
| | | | (-3.33) | |
| $PHI_{t-1}$ *(Large)* | | | | -0.034*** |
| | | | | (-3.10) |
| Controls | Yes | Yes | Yes | Yes |
| Firm FE | Yes | Yes | Yes | Yes |
| Year FE | Yes | Yes | Yes | Yes |
| Observations | 26,228 | 26,228 | 26,228 | 26,228 |
| $R^2$ | 0.152 | 0.152 | 0.152 | 0.152 |

**Panel B: Regressions of Down-to-up Volatility on Alternative PHI Measures**

| Dep. Var. | $DUVOL_t$ | | | |
|---|---|---|---|---|
| | (1) | (2) | (3) | (4) |
| $PHI_{t-1}$ *(Time-invariant)* | -0.030*** | | | |
| | (-2.82) | | | |
| $PHI_{t-1}$ *(Prior)* | | -0.038*** | | |
| | | (-3.34) | | |
| $PHI_{t-1}$ *(Strong)* | | | -0.031*** | |
| | | | (-3.47) | |
| $PHI_{t-1}$ *(Large)* | | | | -0.036*** |
| | | | | (-3.19) |
| Controls | Yes | Yes | Yes | Yes |
| Firm FE | Yes | Yes | Yes | Yes |
| Year FE | Yes | Yes | Yes | Yes |
| Observations | 26,228 | 26,228 | 26,228 | 26,228 |
| $R^2$ | 0.165 | 0.165 | 0.165 | 0.165 |

**Panel C: Baseline Regressions Controlling for the Average Republican Indices of Directors**

| Dep. Var. | $NCSKEW_t$ | $DUVOL_t$ |
|---|---|---|
| | (1) | (2) |
| $PHI_{t-1}$ | -0.024*** | -0.025*** |
| | (-2.99) | (-3.10) |
| $RepIndep_{t-1}$ | 0.009 | 0.005 |
| | (1.15) | (0.66) |
| $Sigma_{t-1}$ | 8.850*** | 4.981*** |
| | (6.97) | (4.41) |
| $Ret_{t-1}$ | 0.240*** | 0.300*** |
| | (12.41) | (15.45) |
| $Dturn_{t-1}$ | -0.002 | -0.003 |
| | (-0.22) | (-0.40) |
| $MB_{t-1}$ | 0.011*** | 0.012*** |
| | (5.36) | (5.70) |
| $Lev_{t-1}$ | -0.224*** | -0.264*** |
| | (-2.99) | (-3.41) |
| $ROA_{t-1}$ | 1.801*** | 2.143*** |
| | (13.44) | (15.63) |
| $LnMV_{t-1}$ | -0.254*** | -0.288*** |
| | (-15.50) | (-17.25) |
| $DA_{t-1}$ | 0.021 | 0.015 |
| | (1.08) | (0.82) |
| $LnBoardSize_{t-1}$ | 0.200*** | 0.214*** |
| | (4.54) | (4.79) |
| $Connection_{t-1}$ | -0.138 | -0.082 |
| | (-0.97) | (-0.56) |
| Firm FE | Yes | Yes |
| Year FE | Yes | Yes |
| Observations | 26,228 | 26,228 |
| $R^2$ | 0.152 | 0.165 |

**Table 4: Regressions of Executives and Directors' Republican Indices on Sinclair Acquisitions**
This table presents the regressions of directors' Republican indices (Column 1) and CEOs' Republic indices (Column 2) on Sinclair acquisitions. *REP* is the Republican index of an individual, calculated as the difference between the individual's dollar amount of donation to Republican recipients and her dollar amount of donation to Democratic recipients divided by her total dollar amount of donation to either Republican recipients or Democratic recipients in an election cycle. *Sinclair* is a dummy variable that equals one if the individual is affected by a Sinclair acquisition in a given year, and zero otherwise. Definitions of all other variables are provided in the Appendix. If a director holds positions in multiples firms in a given year, the firm characteristics are obtained from the firm where the director has served the longest tenure. All regressions include firm and year fixed effects. Robust t-statistics, clustered by firm, are reported in parentheses. *, **, and *** represent statistical significance at the 10%, 5%, and 1% levels, respectively.

| Dep. Var. | $REP_t$ | |
|---|---|---|
| | Directors | CEOs |
| | (1) | (2) |
| $Sinclair_{t-1}$ | 0.020*** | -0.019 |
| | (2.66) | (-0.70) |
| $Sigma_{t-1}$ | 0.149 | -0.344 |
| | (1.05) | (-0.59) |
| $Ret_{t-1}$ | 0.002 | 0.009 |
| | (0.94) | (1.08) |
| $Dturn_{t-1}$ | 0.001 | -0.001 |
| | (0.75) | (-0.44) |
| $MB_{t-1}$ | -0.000 | 0.000 |
| | (-0.86) | (0.05) |
| $Lev_{t-1}$ | 0.004 | -0.086* |
| | (0.30) | (-1.96) |
| $ROA_{t-1}$ | 0.030 | 0.073 |
| | (1.58) | (1.03) |
| $LnMV_{t-1}$ | -0.002 | 0.010 |
| | (-1.04) | (1.02) |
| $DA_{t-1}$ | 0.002 | -0.007 |
| | (0.67) | (-0.91) |
| $LnBoardSize_{t-1}$ | 0.002 | -0.024 |
| | (0.29) | (-0.83) |
| $Connection_{t-1}$ | 0.008 | -0.001 |
| | (0.32) | (-0.01) |
| Firm FE | Yes | Yes |
| Year FE | Yes | Yes |
| Observations | 167,039 | 25,072 |
| $R^2$ | 0.062 | 0.597 |

**Table 5: Crash Risk and Political Homophily: Results from the Three-stage Instrumental Variable Approach**

This table presents the regressions of the crash risk measures on *PHI*, with *PHI* instrumented by *PHISinclair*, the political homophily index constructed using individual directors' Republican indices predicted by the model of Table 4. *NCSKEW* is the negative ratio of the third moment of firm-specific daily returns over the standard deviation of firm-specific daily returns raised to the third power. *DUVOL* is the natural logarithm of the ratio of down-day to up-day standard deviation of firm-specific returns. Definitions of all other variables are provided in the Appendix. All regressions include firm and year fixed effects. Robust t-statistics, clustered by firm, are reported in parentheses. *, **, and *** represent statistical significance at the 10%, 5%, and 1% levels, respectively.

| Dep. Var. | $NCSKEW_t$ | $DUVOL_t$ |
|---|---|---|
| | (1) | (2) |
| $PHI_{t-1}$ | -0.024*** | -0.024*** |
| | (-2.92) | (-3.01) |
| $Sigma_{t-1}$ | 8.845*** | 4.978*** |
| | (6.96) | (4.41) |
| $Ret_{t-1}$ | 0.240*** | 0.300*** |
| | (12.40) | (15.45) |
| $Dturn_{t-1}$ | -0.002 | -0.003 |
| | (-0.22) | (-0.40) |
| $MB_{t-1}$ | 0.011*** | 0.012*** |
| | (5.37) | (5.71) |
| $Lev_{t-1}$ | -0.224*** | -0.264*** |
| | (-2.98) | (-3.41) |
| $ROA_{t-1}$ | 1.803*** | 2.143*** |
| | (13.45) | (15.64) |
| $LnMV_{t-1}$ | -0.254*** | -0.289*** |
| | (-15.52) | (-17.27) |
| $DA_{t-1}$ | 0.021 | 0.015 |
| | (1.08) | (0.82) |
| $LnBoardSize_{t-1}$ | 0.200*** | 0.215*** |
| | (4.55) | (4.79) |
| $Connection_{t-1}$ | -0.138 | -0.081 |
| | (-0.97) | (-0.56) |
| Firm FE | Yes | Yes |
| Year FE | Yes | Yes |
| Observations | 26,228 | 26,228 |

**Table 6: Political Homophily and Returns of Insider Trades**

This table reports the regressions on the relation between insider trading returns and the political homophily index. The sample includes insider purchases made by directors and executives from Thomson Reuter's Insider Data. *Ret0*, *Ret30*, *Ret60*, *Ret90*, and *Ret180* are the market-adjusted returns of an insider's long position for 0, 30, 60, 90, and 180 trading days, respectively (i.e., the return of investing one dollar mimicking the insider trade minus the return of taking the opposite position in the CRSP value-weighted market index). *Independent* is a dummy variable that equals one if an individual is an independent director, and zero otherwise. *TradeSize* is the size of an insider trade, measured by the dollar amount of the trade as a fraction of the firm's market capitalization. Definitions of all other variables are provided in the Appendix. *PHI×Independent×TradeSize*, *PHI×Independent*, *PHI×TradeSize*, and *PHI* are instrumented by *PHISinclair×Independent×TradeSize*, *PHISinclair×Independent*, *PHISinclair×TradeSize*, and *PHISinclair*. All regressions include firm and year fixed effects. Robust t-statistics, clustered by firm, are reported in parentheses. *, **, and *** represent statistical significance at the 10%, 5%, and 1% levels, respectively.

| Dep. Var. | *Ret0* | *Ret30* | *Ret60* | *Ret90* | *Ret180* |
|---|---|---|---|---|---|
| | (1) | (2) | (3) | (4) | (5) |
| *PHI×Independent×TradeSize* | 0.002 | 0.006** | 0.005* | 0.005 | 0.010** |
| | (1.00) | (2.20) | (1.69) | (1.55) | (2.06) |
| *PHI×Independent* | -0.013 | -0.029 | 0.002 | 0.002 | 0.007 |
| | (-0.79) | (-1.31) | (0.07) | (0.08) | (0.23) |
| *PHI×TradeSize* | -0.002 | -0.006** | -0.004 | -0.004 | -0.004 |
| | (-0.82) | (-2.04) | (-1.27) | (-1.36) | (-1.05) |
| *Independent×TradeSize* | -0.007 | -0.027** | -0.020* | -0.024** | -0.046** |
| | (-1.14) | (-2.32) | (-1.89) | (-1.98) | (-2.32) |
| *PHI* | 0.021 | 0.033* | 0.007 | 0.014 | 0.015 |
| | (1.42) | (1.65) | (0.22) | (0.46) | (0.53) |
| *Independent* | 0.049 | 0.097 | -0.038 | -0.037 | -0.061 |
| | (0.75) | (1.14) | (-0.31) | (-0.30) | (-0.59) |
| *TradeSize* | 0.004 | 0.029** | 0.020* | 0.025* | 0.026 |
| | (0.74) | (2.27) | (1.75) | (1.87) | (1.54) |
| *ROA* | -0.146 | -0.142 | -0.096 | -0.058 | 0.215 |
| | (-1.19) | (-1.05) | (-0.42) | (-0.22) | (0.77) |
| *CAPEX* | -0.044 | -0.100* | -0.157** | -0.169* | -0.310*** |
| | (-1.01) | (-1.84) | (-1.99) | (-1.80) | (-2.68) |
| *RD* | -0.049 | 0.102 | 0.483 | 0.769 | 0.979 |
| | (-0.19) | (0.28) | (0.88) | (1.24) | (1.36) |
| *LnAsset* | 0.140*** | 0.119*** | 0.128*** | 0.096** | -0.019 |
| | (4.94) | (4.02) | (3.49) | (2.54) | (-0.38) |
| *Lev* | 0.214 | 0.285* | 0.343 | 0.458* | 0.741*** |
| | (1.30) | (1.73) | (1.45) | (1.86) | (2.63) |
| *LnBoardSize* | 0.122 | 0.067 | 0.058 | 0.073 | -0.122 |
| | (1.12) | (0.64) | (0.41) | (0.48) | (-0.66) |
| *Connection* | -0.044 | 0.014 | 0.144 | 0.225 | 0.422* |
| | (-0.39) | (0.12) | (0.80) | (1.17) | (1.65) |
| Observations | 55,182 | 55,182 | 55,182 | 55,182 | 55,182 |

**Table 7: Political Homophily and the Subsequent Divestitures of Acquired Assets**

This table presents the linear probability regressions of subsequent divestitures of acquired assets. The sample includes completed acquisitions covered by Capital IQ. *Divest* is a dummy variable that equals one if an acquired firm is subsequently divested in the three years after the completion date of the acquisition. *CAR* is the acquirers' three-day cumulative abnormal returns around the announcement dates of the acquisitions, estimated using the market model. Definitions of all other variables are provided in the Appendix. *PHI×CAR* and *PHI* are instrumented by *PHISinclair×CAR* and *PHISinclair*. Columns (1) and (2) include year fixed effects. Columns (3) and (4) include industry (at the two-digit SIC level) and year fixed effects. Robust t-statistics, clustered by firm, are reported in parentheses. *, **, and *** represent statistical significance at the 10%, 5%, and 1% levels, respectively.

| Dep. Var. | *Divest* | | | |
|---|---|---|---|---|
| | (1) | (2) | (3) | (4) |
| *PHI×CAR* | | -0.040** | | -0.036** |
| | | (-2.46) | | (-2.24) |
| *PHI* | | 0.000 | | 0.001 |
| | | (0.16) | | (0.60) |
| *CAR* | -0.039** | 0.117* | -0.037** | 0.104 |
| | (-2.47) | (1.76) | (-2.36) | (1.56) |
| *AcqSize* | 0.003** | 0.003** | 0.002* | 0.002* |
| | (2.49) | (2.49) | (1.96) | (1.94) |
| *AcqMB* | -0.000 | -0.000 | -0.000 | -0.000 |
| | (-0.71) | (-0.71) | (-0.80) | (-0.81) |
| *AcqLev* | -0.010 | -0.010 | -0.008 | -0.008 |
| | (-1.31) | (-1.31) | (-1.26) | (-1.24) |
| *AcqROA* | -0.055*** | -0.054*** | -0.037*** | -0.037*** |
| | (-3.19) | (-3.19) | (-2.90) | (-2.89) |
| *LnDealValue* | -0.000 | -0.000 | -0.000 | -0.000 |
| | (-0.24) | (-0.26) | (-0.18) | (-0.20) |
| *MissingDealValue* | -0.001 | -0.001 | -0.001 | -0.001 |
| | (-0.52) | (-0.55) | (-0.25) | (-0.26) |
| *Hostile* | 0.010 | 0.010 | 0.007 | 0.007 |
| | (0.25) | (0.24) | (0.20) | (0.19) |
| *Stock* | -0.010*** | -0.010*** | -0.011** | -0.011** |
| | (-2.70) | (-2.70) | (-2.28) | (-2.28) |
| *Tender* | 0.022*** | 0.022*** | 0.023*** | 0.024*** |
| | (2.59) | (2.61) | (2.77) | (2.79) |
| Industry FE | No | No | Yes | Yes |
| Year FE | Yes | Yes | Yes | Yes |
| Observations | 21,935 | 21,935 | 21,515 | 21,515 |

**Table 8: Political Homophily and Asset Write-downs**

This table presents the regressions of asset write-downs on the political homophily index. $SPI_t$ is a firm's special items in year *t*, including significant nonrecurring items, asset write-downs, impairments of goodwill, and restructuring charges, scaled by its market capitalization at year *t-1*. $WD_t$ is the sum of a firm's asset write-downs and goodwill impairments in year *t* scaled by its market capitalization at year *t-1*. *BtM* is a firm's book value of assets divided by its market value of assets. Definitions of all other variables are provided in the Appendix. *PHI*×*BtM* and *PHI* are instrumented by *PHISinclair*×*BtM* and *PHISinclair*. All regressions include firm and year fixed effects. Robust t-statistics, clustered by firm, are reported in parentheses. *, **, and *** represent statistical significance at the 10%, 5%, and 1% levels, respectively.

| Dep. Var. | $SPI_t$ | | $WD_t$ | |
|---|---|---|---|---|
| | (1) | (2) | (3) | (4) |
| $PHI_{t-1}\times BtM_{t-1}$ | | -0.018** | | -0.017* |
| | | (-2.01) | | (-1.77) |
| $PHI_{t-1}$ | | 0.047** | | 0.046** |
| | | (2.45) | | (2.39) |
| $BtM_{t-1}$ | -0.444*** | -0.365*** | -0.379*** | -0.312*** |
| | (-22.51) | (-9.01) | (-19.23) | (-7.55) |
| $ROA_{t-1}$ | | 0.028 | | -0.303** |
| | | (0.19) | | (-2.31) |
| $CAPEX_{t-1}$ | | -0.203*** | | -0.279*** |
| | | (-3.08) | | (-4.01) |
| $RD_{t-1}$ | | 0.213 | | 0.814** |
| | | (0.54) | | (2.34) |
| $LnAsset_{t-1}$ | | -0.081*** | | -0.181*** |
| | | (-2.87) | | (-6.51) |
| $Lev_{t-1}$ | | -0.304*** | | -0.106 |
| | | (-2.83) | | (-1.11) |
| $LnBoardSize_{t-1}$ | | 0.025 | | 0.022 |
| | | (0.42) | | (0.37) |
| $Connection_{t-1}$ | | 0.126 | | 0.108 |
| | | (0.74) | | (0.60) |
| Firm FE | Yes | Yes | Yes | Yes |
| Year FE | Yes | Yes | Yes | Yes |
| Observations | 25,520 | 25,520 | 25,520 | 25,520 |

**Table 9: Political Homophily and Risk Taking**

This table presents the regressions of firm's risk-taking measures on the political homophily index. *Lev*, *Vol*, and *IdioVol* are a firm's book leverage, stock return volatility, and idiosyncratic return volatility, respectively. *PHI* is instrumented by *PHISinclair*. Definitions of all other variables are provided in the Appendix. All regressions include firm and year fixed effects. Robust t-statistics, clustered by firm, are reported in parentheses. *, **, and *** represent statistical significance at the 10%, 5%, and 1% levels, respectively.

| Dep. Var. | $Lev_t$ | $Vol_t$ | $IdioVol_t$ |
|---|---|---|---|
| | (1) | (2) | (3) |
| $PHI_{t-1}$ | 0.001 | -0.001 | 0.001 |
| | (0.30) | (-0.08) | (0.14) |
| $ROA_{t-1}$ | -0.080 | -2.176*** | -2.351*** |
| | (-1.01) | (-16.16) | (-16.50) |
| $CAPEX_{t-1}$ | 0.007 | 0.231*** | 0.171*** |
| | (0.17) | (3.90) | (2.84) |
| $RD_{t-1}$ | -0.131 | 0.262 | 0.475 |
| | (-0.54) | (0.65) | (1.11) |
| $LnAsset_{t-1}$ | 0.017 | -0.119*** | -0.180*** |
| | (1.48) | (-5.57) | (-7.94) |
| $Lev_{t-1}$ | 3.660*** | 0.730*** | 0.801*** |
| | (60.88) | (9.75) | (9.96) |
| $LnBoardSize_{t-1}$ | 0.021 | -0.087** | -0.058 |
| | (0.96) | (-2.21) | (-1.40) |
| $Connection_{t-1}$ | 0.020 | 0.013 | -0.004 |
| | (0.27) | (0.11) | (-0.03) |
| Firm FE | Yes | Yes | Yes |
| Year FE | Yes | Yes | Yes |
| Observations | 25,463 | 26,228 | 26,228 |

**Table 10: Crash Risk and Political Homophily: Cross Sectional Analyses Based on Corporate Governance**

This table presents the regressions of crash risk measures on political homophily index in the subsamples of firms based on corporate governance. In Panel A (Panel B), the subsamples are based on whether a firm's institutional ownership (E-index) is above or below the sample median. *NCSKEW* is the negative ratio of the third moment of firm-specific daily returns over the standard deviation of firm-specific daily returns raised to the third power. *DUVOL* is the natural logarithm of the ratio of down-day to up-day standard deviation of firm-specific returns. *PHI* is instrumented by *PHISinclair*. Definitions of all other variables are provided in the Appendix. All regressions include firm and year fixed effects. Robust t-statistics, clustered by firm, are reported in parentheses. *, **, and *** represent statistical significance at the 10%, 5%, and 1% levels, respectively.

**Panel A: Regressions of Crash Risk on Political Homophily: Subsamples Based on Institutional Ownership**

| Dep. Var. | $NCSKEW_t$ | | $DUVOL_t$ | |
|---|---|---|---|---|
| | High IO | Low IO | High IO | Low IO |
| | (1) | (2) | (3) | (4) |
| $PHI_{t-1}$ | -0.036*** | -0.015 | -0.041*** | -0.012 |
| | (-2.71) | (-1.45) | (-3.17) | (-1.13) |
| $Sigma_{t-1}$ | 13.522*** | 4.908*** | 8.171*** | 2.294 |
| | (6.08) | (3.05) | (4.27) | (1.56) |
| $Ret_{t-1}$ | 0.281*** | 0.252*** | 0.350*** | 0.313*** |
| | (8.46) | (10.11) | (10.88) | (12.29) |
| $Dturn_{t-1}$ | -0.012 | 0.000 | -0.011 | -0.004 |
| | (-1.07) | (0.03) | (-1.03) | (-0.39) |
| $MB_{t-1}$ | 0.013*** | 0.009*** | 0.015*** | 0.011*** |
| | (4.38) | (3.26) | (4.66) | (3.36) |
| $Lev_{t-1}$ | -0.253** | -0.141 | -0.251** | -0.236** |
| | (-2.20) | (-1.24) | (-2.18) | (-2.05) |
| $ROA_{t-1}$ | 1.837*** | 1.721*** | 2.207*** | 2.035*** |
| | (8.73) | (9.77) | (10.44) | (10.91) |
| $LnMV_{t-1}$ | -0.338*** | -0.248*** | -0.386*** | -0.282*** |
| | (-12.57) | (-11.70) | (-14.80) | (-12.93) |
| $DA_{t-1}$ | 0.037 | -0.003 | 0.024 | 0.000 |
| | (1.23) | (-0.10) | (0.88) | (0.00) |
| $LnBoardSize_{t-1}$ | 0.248*** | 0.183*** | 0.304*** | 0.173*** |
| | (3.39) | (2.95) | (4.16) | (2.72) |
| $Connection_{t-1}$ | -0.146 | -0.095 | -0.081 | -0.073 |
| | (-0.60) | (-0.54) | (-0.34) | (-0.37) |
| Firm FE | Yes | Yes | Yes | Yes |
| Year FE | Yes | Yes | Yes | Yes |
| Observations | 12,889 | 12,837 | 12,889 | 12,837 |

**Panel B: Regressions of Crash Risk on Political Homophily: Subsamples Based on E-index**

| Dep. Var. | $NCSKEW_t$ | | $DUVOL_t$ | |
|---|---|---|---|---|
| | High E-index | Low E-index | High E-index | Low E-index |
| | (1) | (2) | (3) | (4) |
| $PHI_{t-1}$ | -0.005 | -0.026** | -0.012 | -0.023** |
| | (-0.35) | (-2.26) | (-0.77) | (-2.04) |
| $Sigma_{t-1}$ | 9.489*** | 8.286*** | 4.952*** | 4.841*** |
| | (4.44) | (5.05) | (2.68) | (3.24) |
| $Ret_{t-1}$ | 0.311*** | 0.241*** | 0.382*** | 0.302*** |
| | (10.11) | (9.27) | (12.59) | (11.34) |
| $Dturn_{t-1}$ | -0.005 | 0.002 | -0.009 | 0.004 |
| | (-0.40) | (0.21) | (-0.78) | (0.43) |
| $MB_{t-1}$ | 0.016*** | 0.008*** | 0.017*** | 0.011*** |
| | (4.17) | (3.04) | (4.23) | (3.78) |
| $Lev_{t-1}$ | -0.317** | -0.208** | -0.335*** | -0.264** |
| | (-2.53) | (-2.02) | (-2.61) | (-2.51) |
| $ROA_{t-1}$ | 2.320*** | 1.853*** | 2.680*** | 2.173*** |
| | (10.15) | (10.86) | (11.79) | (11.89) |
| $LnMV_{t-1}$ | -0.340*** | -0.239*** | -0.369*** | -0.287*** |
| | (-11.63) | (-10.61) | (-12.63) | (-12.20) |
| $DA_{t-1}$ | 0.058** | 0.011 | 0.042 | 0.006 |
| | (2.06) | (0.41) | (1.55) | (0.21) |
| $LnBoardSize_{t-1}$ | 0.182** | 0.223*** | 0.197** | 0.256*** |
| | (2.19) | (3.66) | (2.40) | (4.09) |
| $Connection_{t-1}$ | -0.066 | -0.466* | -0.052 | -0.369 |
| | (-0.31) | (-1.94) | (-0.26) | (-1.51) |
| Firm FE | Yes | Yes | Yes | Yes |
| Year FE | Yes | Yes | Yes | Yes |
| Observations | 12,478 | 13,344 | 12,478 | 13,344 |

**Table 11: Political Homophily Index and CEO Turnover-performance Sensitivity**

This table reports the linear probability regressions of CEO turnovers on firms' stock returns. *Turnover* is a dummy variable that equals one if a firm experiences a CEO turnover in a given year, and zero otherwise. *Ret* is a firm's cumulative stock returns in the past four years. *PHI*×*Ret* and *PHI* are instrumented by *PHISinclair*×*Ret* and *PHISinclair*. Definitions of all other variables are provided in the Appendix. Columns (1) and (2) report the regressions in the full sample. Columns (3) to (6) (Columns (7) and (10)) report the regressions in subsamples based on whether a firm's institutional ownership (E-index) is above or below the sample median. All regressions include firm and year fixed effects. Robust t-statistics, clustered by firm, are reported in parentheses. *, **, and *** represent statistical significance at the 10%, 5%, and 1% levels, respectively.

| Dep. Var. | $Turnover_{t+1}$ | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | | | Institutional ownership | | | | E-index | | | |
| | Full sample | | High | | Low | | High | | Low | |
| | (1) | (2) | (3) | (4) | (5) | (6) | (7) | (8) | (9) | (10) |
| $PHI_t \times Ret_{(t-3,t)}$ | | 0.059** | | -0.018 | | 0.119*** | | 0.084*** | | 0.040 |
| | | (2.28) | | (-0.50) | | (3.01) | | (2.69) | | (0.74) |
| $PHI_t$ | | -0.008 | | 0.004 | | -0.013* | | -0.004 | | -0.005 |
| | | (-1.50) | | (0.58) | | (-1.69) | | (-0.31) | | (-0.75) |
| $Ret_{(t-3,t)}$ | -0.115*** | -0.325*** | -0.095** | -0.030 | -0.114*** | -0.532*** | -0.097 | -0.235 | -0.120*** | -0.412*** |
| | (-4.14) | (-3.32) | (-2.35) | (-0.22) | (-2.79) | (-3.53) | (-1.61) | (-1.10) | (-3.57) | (-3.50) |
| $RetireAge_t$ | 0.101*** | 0.101*** | 0.121*** | 0.121*** | 0.092*** | 0.095*** | 0.033 | 0.034 | 0.109*** | 0.110*** |
| | (5.89) | (5.91) | (4.36) | (4.37) | (3.82) | (3.98) | (0.90) | (0.94) | (4.85) | (4.87) |
| $LnTenure_t$ | 0.238*** | 0.237*** | 0.256*** | 0.256*** | 0.258*** | 0.258*** | 0.308*** | 0.308*** | 0.287*** | 0.287*** |
| | (19.56) | (19.51) | (13.82) | (13.83) | (14.59) | (14.46) | (8.93) | (8.90) | (17.19) | (17.18) |
| $LnAsset_t$ | 0.025** | 0.025** | 0.016 | 0.016 | 0.022 | 0.022 | 0.031 | 0.031 | 0.005 | 0.005 |
| | (2.34) | (2.32) | (1.03) | (1.04) | (1.38) | (1.40) | (1.26) | (1.27) | (0.36) | (0.40) |
| $MB_t$ | -0.001 | -0.001 | 0.002 | 0.002 | -0.003 | -0.003 | 0.004 | 0.004 | -0.001 | -0.001 |
| | (-0.35) | (-0.36) | (0.88) | (0.88) | (-1.27) | (-1.26) | (1.08) | (1.08) | (-0.70) | (-0.68) |
| $DividendPay_t$ | 0.012 | 0.012 | -0.000 | -0.000 | 0.019 | 0.018 | 0.032 | 0.032 | -0.002 | -0.001 |
| | (0.79) | (0.77) | (-0.02) | (-0.02) | (0.79) | (0.72) | (1.22) | (1.22) | (-0.09) | (-0.07) |
| Firm FE | Yes | Yes | Yes | Yes | Yes | Yes | Yes | Yes | Yes | Yes |
| Year FE | Yes | Yes | Yes | Yes | Yes | Yes | Yes | Yes | Yes | Yes |
| Observations | 12,006 | 12,006 | 5,843 | 5,843 | 5,851 | 5,851 | 5,695 | 5,695 | 5,962 | 5,962 |

**Table 12: Political Homophily and Tobin's Q**

This table presents the regressions of Tobin's Q on the political homophily index. Tobin's Q is calculated as the ratio of a firm's market value of assets to its book value of assets. *PHI* is instrumented by *PHISinclair*. Definitions of all other variables are provided in the Appendix. Column (1) reports the regression in the full sample. Columns (2) and (3) (Columns (4) and (5)) report the regressions in subsamples based on whether a firm's institutional ownership (E-index) is above or below the sample median. All regressions include firm and year fixed effects. Robust t-statistics, clustered by firm, are reported in parentheses. *, **, and *** represent statistical significance at the 10%, 5%, and 1% levels, respectively.

| Dep. Var. | *Tobin's* $Q_t$ | | | | |
|---|---|---|---|---|---|
| | Full sample | High IO | Low IO | High E-index | Low E-index |
| | (1) | (2) | (3) | (4) | (5) |
| $PHI_{t-1}$ | -0.013** | -0.006 | -0.016* | -0.012* | -0.005 |
| | (-2.08) | (-0.66) | (-1.87) | (-1.87) | (-0.66) |
| $ROA_{t-1}$ | 3.164*** | 3.259*** | 2.926*** | 3.261*** | 3.630*** |
| | (18.30) | (13.90) | (11.63) | (13.49) | (15.93) |
| $CAPEX_{t-1}$ | 1.072*** | 0.923*** | 1.223*** | 0.583*** | 0.648*** |
| | (14.13) | (9.38) | (11.02) | (7.71) | (7.37) |
| $RD_{t-1}$ | 1.930*** | 1.198 | 2.207** | 2.627*** | 2.110** |
| | (3.03) | (1.62) | (2.40) | (3.47) | (2.49) |
| $LnAsset_{t-1}$ | -0.074*** | -0.087** | -0.083** | -0.256*** | -0.277*** |
| | (-3.34) | (-2.55) | (-2.24) | (-8.79) | (-9.34) |
| $Lev_{t-1}$ | 0.020 | 0.118 | 0.059 | -0.110 | -0.129 |
| | (0.26) | (1.07) | (0.54) | (-0.97) | (-1.26) |
| $LnBoardSize_{t-1}$ | -0.255*** | -0.245*** | -0.188*** | -0.036 | -0.153*** |
| | (-5.82) | (-4.48) | (-2.85) | (-0.66) | (-2.83) |
| $Connection_{t-1}$ | 0.022 | -0.164 | 0.140 | -0.043 | 0.235 |
| | (0.19) | (-1.18) | (0.81) | (-0.35) | (1.34) |
| Firm FE | Yes | Yes | Yes | Yes | Yes |
| Year FE | Yes | Yes | Yes | Yes | Yes |
| Observations | 26,228 | 12,889 | 12,837 | 12,478 | 13,344 |

**Appendix: Definition of variables**

| Variables | Definition |
|---|---|
| *NCSKEW* | Negative ratio of the third moment of firm-specific daily returns over the standard deviation of firm-specific daily returns raised to the third power, calculated using Equation (4) |
| *DUVOL* | Natural logarithm of the ratio of down-day to up-day standard deviation of firm-specific returns, calculated using Equation (5) |
| *PHI* | Political homophily index between a firm's CEO and independent directors, calculated using Equation (2) |
| *PHISinclair* | Political homophily index between a firm's CEO and independent directors, constructed using director Republican indices predicted by Sinclair acquisitions. |
| *RepCEO* | Republican index of a firm's CEO, calculated using Equation (1). |
| *RepIndep* | Average Republican index of a firm's independent directors, calculated using Equation (1). |
| *Sigma* | The yearly standard deviation of a firm's daily firm-specific stock returns. |
| *Ret* | Cumulative firm-specific daily returns in a given year. |
| *Dturn* | Average monthly share turnover in year *t* minus the average monthly share turnover in year *t-1*. |
| *MB* | Market-to-book ratio, defined as market value of equity (PRCC_F×CSHO) divided by book value of equity (CEQ). |
| *Lev* | Book leverage, defined as book value of long-term debt (DLTT) divided by total assets (AT). |
| *ROA* | Return on assets, defined as operating income before depreciation (OIBDP) divided by book value of assets (AT). |
| *LnMV* | Natural logarithm of market value of equity (PRCC_F×CSHO). |
| *DA* | Absolute value of discretionary accruals, estimated using the Jones (1991) model. |
| *LnBoardSize* | Natural logarithm of the number of directors in a firm. |
| *Connection* | Percentage of a firm's directors who are socially connected to the CEO, constructed following Dasgupta, Zhang, and Zhu (2015). |
| *PHI (Time-invariant)* | Political homophily index constructed using the individuals' Republican index based on their total amount of contribution up to the year 2019. |
| *PHI (Prior)* | Political homophily index constructed using the individuals' historic Republican index (i.e., for each individual *p* in year *t*, the Republican index calculated using her historic contribution made before year *t*). |
| *PHI (Strong)* | Political homophily index constructed using the Republican index of the individuals whose differences in contributions to the two parties exceed $2,000 in the election cycle. |
| *PHI (Large)* | Political homophily index constructed using the Republican index of the individuals whose historical total amounts of contribution exceed $2,000. |
| *Sinclair* | A dummy variable that equals one if a director or CEO is affected by a Sinclair acquisition in her county of residence in a given year, and zero otherwise |
| *Ret0* | The market adjusted return of an insider's purchase for 0 trading days (i.e., the return of investing one dollar mimicking the insider trade minus the return of taking the opposite position in the CRSP value-weighted market index). |
| *Ret30* | The market adjusted return of an insider's purchase for 30 trading days (i.e., the return of investing one dollar mimicking the insider trade minus the return of taking the opposite position in the CRSP value-weighted market index). |

| | |
|---|---|
| *Ret60* | The market adjusted return of an insider's purchase for 60 trading days (i.e., the return of investing one dollar mimicking the insider trade minus the return of taking the opposite position in the CRSP value-weighted market index). |
| *Ret90* | The market adjusted return of an insider's purchase for 90 trading days (i.e., the return of investing one dollar mimicking the insider trade minus the return of taking the opposite position in the CRSP value-weighted market index). |
| *Ret180* | The market adjusted return of an insider's purchase for 180 trading days (i.e., the return of investing one dollar mimicking the insider trade minus the return of taking the opposite position in the CRSP value-weighted market index). |
| *Independent* | A dummy variable that equals one if an trading insider is an independent director, and zero otherwise. |
| *TradeSize* | Size of an insider transaction, defined as the fraction of the firm's market capitalization. |
| *CAPEX* | Capital expenditure (CAPX) divided by net property, plant, and equipment (PPENT). |
| *RD* | Research and development expenses (XRD) divided by total assets (AT). |
| *LnAsset* | Natural logarithm of book value of total assets (AT). |
| *Divest* | A dummy variable that equals one if the acquired firm in a transaction is subsequently divested in the three years after the completion date of the acquisition. |
| *CAR* | An acquirer's three-day cumulative abnormal return around the announcement date of transaction, estimated using the market model. |
| *AcqSize* | Natural logarithm of an acquirer's total assets. |
| *AcqMB* | Market-to-book ratio of an acquirer. |
| *AcqLev* | Book leverage of an acquirer. |
| *AcqROA* | Return on assets of an acquirer. |
| *LnDealValue* | Natural logarithm of the transaction size of an acquisition, set to zero if missing. |
| *MissingDealValue* | A dummy variable that equals one if the transaction value is missing, and zero otherwise. |
| *Hostile* | A dummy variable that equals one if an acquisition is flagged as hostile in the Capital IQ database, and zero otherwise. |
| *Stock* | A dummy variable that equals one if an acquisition is flagged as a stock merger in the Capital IQ database, and zero otherwise. |
| *Tender* | A dummy variable that equals one if an acquisitions is flagged as an tender offer in Capital IQ database, and zero otherwise. |
| *SPI* | A firm's special items (SPI) in year *t* divided by the firm's market capitalization (PRCC_F×CSHO) at the end of year *t-1*. |
| *WD* | A firm's asset write-downs (WDP) and goodwill impairments (GDWLIP) in year *t* divided by the firm's market capitalization (PRCC_F×CSHO) at the end of year *t-1*. |
| *BtM* | Total assets (AT) divided by the sum of market capitalization (PRCC_F×CSHO) plus total assets (AT) minus the book value of common equity (CEQ). |
| *Vol* | Standard deviation of a firm's daily stock returns in a given year. |
| *IdioVol* | Idiosyncratic stock return volatility, estimated using the Fama-French three-factor model. |
| *Turnover* | A dummy variable that equals one if a firm experiences a CEO turnover in a given year, and zero otherwise. |
| *RetireAge* | A dummy variable that equals one if a CEO is above 65-year-old, and zero otherwise. |
| *LnTenure* | Natural logarithm of a CEO's tenure. |

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| *DividendPay* | A dummy variable that equals one if a firm pays dividend in a given year, and zero otherwise. |
| *Tobin's Q* | Tobin's Q, defined as market value of equity (PRCC_F×CSHO) plus book value of assets (AT) minus book value of equity (CEQ) minus deferred taxes (TXDB, set to zero if missing) divided by book value of assets. |

## about ECGI

The European Corporate Governance Institute has been established to improve *corporate governance through fostering independent scientific research and related activities.*

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