Executive Gatekeepers: Useful and Divertable Governance
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Abstract
We study the effectiveness of internal gatekeepers and then ask whether equity incentives divert the attention of corporate lawyers from gatekeeping. We find that executive gatekeepers reduce compliance failures (AAERS and insider trading profits) to negligible levels and decrease securities fraud and uncaught accounting fraud by 43% and 9% respectively. A general counsel fixed effect explains 12% of the variation in insider trading profits, 7% in AAERS, and 6% in class action suits, over and above firm, year, and CEO fixed effects. Then, using the assumption that gatekeepers hired from law firms are initially less responsive to incentive pay as compared to those hired from other corporations for identification, we find that equity incentives given to gatekeepers unwind some governance improvements. A one standard deviation increase in gatekeeper’s compensation delta unwinds 82% of the prevention of securities fraud. Gatekeepers do not get diverted, however, from frauds associated with regulatory compliance. We conclude with an alternative interpretation of our design that these gatekeepers-in-residence may be hired as value-creators, but totems of governance.

Copies of the paper are available in the department office (BUS 4-20A) or by calling the department at 780-492-5429 or e-mailing sprovost@ualberta.ca.