



Reprimanding Sanction, Management Demography and Turnover: Evidence from a Transitional Economy

Louis T. W. Cheng,^a T. Y. Leung^b

^a School of Accounting and Finance, Hong Kong Polytechnic University

^b Lee ShauKee School of Business and Administration, Open University of Hong Kong

Abstract: The literature shows the importance of top management and board characteristics on firm performance. We extend this literature by examining top management turnover for financially distressed firms. China has a unique sanction rule, which publicly labels financially distressed listed firms to provide the market with a warning signal. Controlling for board characteristics and governance, we evaluate how relational management demography affects turnover of financially distressed firms in China. Our results first show that the demographic characteristics of top management for distressed firms differ from those of normal firms. Second, management turnover is positively related to financial distress. Finally, we show that the departure of either the chairperson or CEO depends on their demographic differences. We conjecture that our findings provide support to the upper echelons theory and scapegoat argument.

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1. Introduction

The literature on management demography, board governance and turnover mainly focuses on their relations with firm performance. We believe that an interesting follow-up research question is how management turnover can be related to leadership characteristics (including both top managers' and board members'). In this study, we empirically examine when firms face financial distress, do boards exhibit a systematic preference in top management replacement?

We are motivated to use financial distress firms in China (i.e. listed firms with a special treatment (ST) status) to examine the relation between management demography and turnovers for two reasons. First, the government has reprimanding sanction against financially distress firms by labeling them with a ST code that is intended to provide a risk warning to the market. Such a ST warning rule to protect the interests of shareholders and investors is not common in other countries around the world, particularly in emerging markets. Thus, using these Chinese firms allows us to understand how such a sanction regulation may affect turnover decisions in developing countries.

Second, China provides an interesting setting for this study. Despite its rapid economic growth, the development of the financial infrastructure and regulatory system are still immature. The Chinese market is characterized with concentrated ownership by controlling shareholders and a weak legal institutional environment. In such a kind of legal environment, investor protection is inadequate, leading to ineffective external control mechanism and poor corporate governance (La Porta et al., 1999). Since the Chinese market lacks an adequate investor protection system and external market for corporate control, a government-imposed disciplinary system with warning to the market seems appropriate.

Consequently, as this publicly known ST status is a result of poor management and/or governance, top management should be accountable. In short, using these Chinese ST firms to examine the leadership turnover related to financial distress can shed insight on how far the Western-style of dismissing the management with poor performance is practiced in China.

First, using the insights from upper echelons theory, we explore how the characteristics of top management and board can shape organizational outcomes, and in our case, poor performance and governance resulting in ST status. More specifically, we hypothesize that the demographic characteristics (age, tenure, education level, title) of top management (chairperson and CEO) are related to corporate performance (Chan et al., 2011; Cheng et al., 2010) and governance, therefore ST status. Our findings show that the chairperson's age and title as well as

the CEO's tenure and education are negatively related to the incidence of reprimanding sanction. Collectively, these results demonstrate that the probability of reprimanding sanction is higher when the chairperson is younger and without professional title. The same is true when the CEO has shorter tenure and less education.

Next, as management turnover can be a direct outcome of corporate governance (Shleifer and Vishny, 1997), we assess if the quality of management is related to the probability of voluntary management turnover. We find that chairperson voluntary turnover is positively related to chairperson's age and CEO's education; and negatively related to education level and title ownership of chairperson and CEO's tenure. This finding raises an interesting question. If management demography and incidence of reprimanding sanction jointly affect the probability of turnover, then what factors determine the turnover choice: chairperson versus CEO. In order to answer this question, we conduct the third test.

Our final research question examines how relational management demography and board governance may affect the choice of forced turnover (chairperson versus CEO). For a firm with good governance practice, top management with poor performance and governance practice should be dismissed. By using the ST-turnover subsample as a proxy of forced turnover¹, we examine if the CEO is being used as the scapegoat and if so, under what circumstances in terms of demographic combinations.

Our paper contributes to the literature on corporate governance and monitoring activities of firms in a transitional economy. It is a challenge to measure the effectiveness of corporate governance mechanism. We make use of the incidence of reprimanding sanctions to examine if the Chinese firms under financial distress have a higher propensity to replace their poorly performing top executives. Our findings generate implications for boards and investors on what would happen to top management when firms are under financial distress in China. Our finding lends support for the regulatory role of improving corporate governance in China. We add to the turnover literature that, besides profitability, reprimanding sanctions from regulatory bodies is also a significant factor relating to turnover. International firms should find such a result useful in deploying their executives in China. In addition, overseas stock market investors considering investments in China should also find our results helpful when making portfolio decision in selecting Chinese stocks.

¹Owing to the problem of forced turnover classification in the literature, we use a new approach to classify forced turnover. The detailed discussion is listed in the Sample Description section.

2. Background and Hypotheses Development

2.1 Reprimanding Sanction - Special Treatment (ST) Announcements

In 2002, the US launched the SOX reform to better enforce the corporate responsibilities and reporting disclosures of US listed firms. However, back to 1998, the China Securities Regulatory Commission (CSRC) already established a disclosure requirement to provide a risk warning to protect the interest of shareholders and investors. When there are adverse financial conditions or other aspects relating to the Chinese listed firms which expose the stocks to the risk of delisting or impede the investors from making appropriate investment judgment, the Shanghai and Shenzhen stock exchanges are required to put the stocks under special treatment (ST).²

The stock exchanges put the stocks under ST in two situations: (1) a warning of the risk of listing termination (delisting risk warning); and (2) other kinds of special treatment. The stocks under delisting risk warning are tagged with “*ST” while the stocks under other kinds of special treatment are required to add “ST” before their short names. The purpose of putting a prefix of *ST or ST before the short name is to make a distinction from other stocks, so that the investors can easily recognize those stocks, which are under ST. In addition, the *ST and ST stocks are also subject to certain trading restrictions. There is a five percent daily up and down price limit for *ST and ST stocks, as compared to a 10% limit for other stocks.³ We make use of the incidence of reprimanding sanction to evaluate what type of leaders (chairperson and CEO) can put the firms at risk. In addition, we also examine the subsequent turnover of the poorly performing top management who leads the road to reprimanding sanction.

2.2 Management Demography

The resource-based view of firm (RBV) argues that the competitive advantage of a firm depends on its utilization of resources to achieve efficiency (Barney, 1991). Hitt et al. (2001) further suggest that human capital is an essential intangible asset for firm operation. Human capital includes expertise, experience, knowledge, and reputation (Coleman, 1988). Social capital is defined as “the sum of actual and potential resources embedded within available through and derived from the network of relationships” (Nahapiet and Ghoshal, 1998, p. 243). Burt (1997) and Hillman and Dalziel (2003) propose that both human capital and social capital are important resources for value creation of a firm.

²The sources of information about special treatment are from “Rules Governing the Listing of Stocks on Shanghai Stock Exchange” and “Rules Governing the Listing of Stocks on Shenzhen Stock Exchange”.

³In this study, we do not distinguish *ST and ST firms, but group them together as “ST firms” which are under reprimanding sanction.

The upper echelons theory (Hambrick, 2007) suggests that the demographic characteristics of top executives are important in shaping organizational outcomes for better or worse. The organization learning and resource-based theories suggest that age and tenure are valuable intangibles as knowledge and experience can enrich human capital and increase with performance (Reed and DeFillippi, 1990). Education level is related to the capacity for information processing (Hambrick and Mason, 1984; Herrmann and Datta, 2002). In addition to these three traditional demographic characteristics, recently, reputation or title is shown to be an important factor affecting corporate decisions (Chan et al., 2011; Francis et al., 2008).

Cyert and March (1963) define top management team (TMT) as the dominant coalition of individuals responsible for firm operation. The interactions between top management as a team through dynamic process strengthen group cohesiveness and affect performance and strategic choices (Iaquinto and Fredrickson, 1997; Smith et al., 1994). TMT literature shows that performance and growth are related to top management team characteristics such as team size, age, experience, and education level (Bantel and Jackson, 1989; Wiersema and Bantel, 1992). Chan et al. (2011) show that the relational demographic homogeneity of chairperson and CEO in terms of title possession and performance is positively related.

2.3 Management Turnover

Owing to the visibility of CEO involuntary dismissal, increased attention has been paid to the relation between poor performance and CEO turnover (Denis and Kruse, 2000; Wiersema, 2002; Zhang, 2008). The agency theory suggests that dismissing a poorly performing CEO is a necessary condition of good governance, and hence sensitivity of management turnover to performance is a measure of governance quality (Shleifer and Vishny, 1989, 1997). In the RBV literature, Barney (1991) refers to human resources as intangible, valuable, unique, inimitable and non-substitutable resource endowments for developing sustainable competitive advantage of a firm. If the resources cannot add value to the firm to develop sustainable competitive advantage, the resources should not be retained (Sirmon et al., 2007). Therefore, management turnover is equivalent to divestiture of unnecessary resources, which is no longer useful for value creation.

A number of studies have shown that poor performance leads to forced managerial turnovers, which are followed by improved performance (Denis and Denis, 1995; Huson et al., 2004; Huson et al., 2001; McNeil et al., 2004; Volpin, 2002). DeFond and Hung (2004) provide evidence from 33 countries that performance-CEO turnover sensitivity is stronger in countries where law enforcement is stronger. Using data from 47 countries between 1992 and

2003, Lei and Miller (2008) find that CEO turnover-performance sensitivity is stronger for cross-listed firms and strongest in countries with weak investor protection.

2.4 Hypotheses

We examine the relation between management demography and reprimanding sanction in the first hypothesis. Our second hypothesis focuses on how management demography may affect the choice of management turnovers.

Hypothesis 1: Incidence of reprimanding sanction and management demography

The upper echelons theory (Hambrick, 2007) and the RBV (Hitt et al., 2001) suggest that top management is an essential element, which influences how firms are managed. In this study, we focus on the two highest-rank top management positions of the firm in China: chairperson and CEO. Burt (1997, p. 339) suggests “while human capital is surely necessary to success, it is useless without the social capital of opportunities in which to apply it.” Cheng et al. (2010) and Chan et al. (2011) find that the demographic characteristics of chairpersons and relational demographic differences between chairperson and CEO in the Chinese firms exert influences on corporate performance. These arguments suggest that the quality of top executives is important in shaping organizational outcomes for better or worse. Using the incidence of reprimanding sanction (ST status), which indicates poor performance and governance, we hypothesize that, the demography (age, tenure, education level, title) of top management is related to organizational outcomes, therefore ST status.

H1: Reprimanding sanction is related to top management demography.

In this study, we examine four demographic characteristics (tenure, age, education level and professional title). The organization learning theory and RBV argue that age and tenure are valuable intangibles as the enriched knowledge and experience built up in life and workplace facilitate the top management to have better understanding to lead the firms more effectively (Reed and DeFillippi, 1990). Hence, we expect that tenure and age of top management to be negatively related to the incidence of reprimanding sanction. Education facilitates the development of intellectual competence, which is important for enhancing capacity for information processing and generating managerial skills in the self-directed learning process (Herrmann and Datta, 2002; Waijerdasak and Suehiro, 2004). Education level is expected to be negatively related to the incidence of reprimanding sanction.

Combining the bridging and bonding perspectives in the social capital literature, social capital is defined as social relation, influence and commonality available to individuals (Adler and Kwon, 2002). Besides human capital (which can be obtained from experience (age and tenure) and education), the social capital literature argues that social capital (or network) is also important to affect performance (Adler and Kwon, 2002; Shipilov and Danis, 2006; Steier and Greenwood, 2000). Coleman (1988) construes that social capital as a value is created through instrumental relationships among people, and Cowen and Marcel (2011) interpret that social capital can be derived from professional competency and business relationships. Therefore, society's membership such as membership to professional bodies can be a measure of social capital. Therefore, we expect that the ownership of professional title held by top management is negatively related to the incidence of reprimanding sanction.

Hypothesis 2: Management demography and turnovers

Our hypothesis 2 is divided into two tests. The first one examines voluntary turnovers and the second one evaluates forced turnovers.

H2: Turnover is related to top management demography.

Dalton et al. (1981) and McElroy et al. (2001) distinguish turnovers between functional turnover (dismissal to force poor performer to leave) and dysfunctional turnover (quit to describe the departure of good performers).⁴ For whatever types of turnover, turnover is linked to firm performance, which is related to management quality.⁵ Our first test of H2 evaluates the relation between management demography and voluntary turnover. We propose that, based on the upper echelons argument that various management characteristics including age should affect performance, management demography and voluntary turnover should be related.

Our second test of H2 focuses on forced turnovers. According to agency theory, top management is accountable for firm performance (Fama, 1980). Consequently, the poorly-performing top management should be removed. Shleifer and Vishny (1989; 1997) argue that dismissing poorly performing CEO is a necessary condition of good governance. As an

⁴Turnovers can also be differentiated by voluntary turnovers due to retirement, contract expiration or resignation and forced turnovers due to dismissal. In this study, functional turnover is equated with forced turnover and dysfunctional turnover is equated with voluntary turnover.

⁵If the firm has good performance, there may be a possibility for the top management to quit (voluntary or dysfunctional turnover) as they may be head-hunted by other firms. The possession of greater human capital increases the mobility in the labor market (Iverson and Buttigieg, 1999). If the firm has poor performance, the top management is likely to be blamed for being incompetent or having poor judgment, leading to dismissal (Kesner and Dalton, 1994; McEvoy and Cascio, 1987). Parrino (1997, p. 176), in the examination of voluntary and involuntary turnovers, suggests that a lack of important human capital may have contributed to their poor performance and consequently to their departure.

explanation for the relation between forced turnovers and performance, the scapegoat hypothesis argues that executives may be used as convenient scapegoats to be dismissed for public relation reason to signal that the firms have “fixed” the problem (Khanna and Poulsen, 1995). In addition, the removal of scapegoats provides a symbolic reassurance that the firms have no tolerance for poor performers (Pfeffer, 1981).

The “ST” labels before their short names provide a signal to the market that the firms have the risk of delisting and adverse financial conditions. Consequently, the top management leading the firm to be under reprimanding sanction should be dismissed. We expect that management turnover should be positively related to the incidence of reprimanding sanction. In addition, we examine how the quality of top management affects the choice of forced turnover (chairperson versus CEO). By using the ST-turnover subsample as a proxy of forced turnover, we examine if CEO is being used as scapegoat and if so, under what circumstances in terms of demographic combinations.

3. Research Method

Our study is of two-fold. First, we examine what types of top management characteristics lead the firms to be under reprimanding sanctions. Next, we identify the determinants of chairperson and CEO turnovers.

3.1 Models

Given the binary nature of the dependent variables in equations (1), (2a) and (2b), we employ logit regression analyses to test H1 and H2. Equation (1) is used to test the relations between management demographic quality and incidence of reprimanding sanction (special treatment (*ST*)) as proposed in H1:

$$ST_{t+1} = \alpha_0 + \Omega_1 Quality_t + \Omega_2 Governance(Control)_t + \Omega_3 Firm(Control)_t + \Omega_4 Year_t + \Omega_5 Industry_j \quad (1)$$

Equations (2a) and (2b) are used to test the relations between management turnover, incidence of reprimanding sanction and management demographic quality as proposed in H2:

$$Turnover_{t+1} = \alpha_0 + \beta_1 ST_t + \Omega_2 Quality_t + \Omega_3 Governance(Control)_t + \Omega_4 Firm(Control)_t + \Omega_5 Year_t + \Omega_6 Industry_j \quad (2a)$$

$$\begin{aligned} Turnover_{t+1} = & \alpha_0 + \beta_1 ST_t + \Omega_2 Quality_t + \Omega_3 ST_t * Quality_t \\ & + \Omega_4 Governance(Control)_t + \Omega_5 Firm(Control)_t + \Omega_6 Year_t + \Omega_7 Industry_j \end{aligned} \quad (2b)$$

3.2 Measurement

Key variables

ST is a dummy coded 1 if the firm is under special treatment status and 0, otherwise. *Turnover* is a dummy coded 1 if there is a change in the position and 0, otherwise. *Quality* represents the different demographic characteristics of top management. *CH* is the prefix to represent the characteristic of a chairperson. *CEO* is the prefix to represent the characteristic of a CEO. Coleman (1988) defines human capital to include expertise, experience, knowledge, reputation and skills, which are derived from position, training and career history.

In this paper, the characteristics include age (Barker and Mueller, 2002; Zhang and Rajagopalan, 2004), tenure (Brookman and Thistle, 2009; Zhang and Rajagopalan, 2003), education level (Herrmann and Datta, 2002) and title (Cheng et al., 2010). *Age* is the age. *Tenure* is the number of years staying in office. We use *Age* and *Tenure* as proxies of experience and power, respectively. *Education*, which is the measure of knowledge and skills, counts the number of schooling with three years for college education, four years for university education, six years for master degree and nine years for Ph.D degree. *Title* is a dummy coded 1 for the ownership of professional title (e.g., accountant, engineer) and 0 otherwise. We use *Title*, which is proxied by professional qualification, to measure expertise, reputation and potential resources available through the network of professionals. Besides examining the demographic quality of chairperson and CEO separately, following Chan et al. (2011), we also measure the relational demography of top management team (TMT). *CHTenure-CEOTenure* is the tenure difference with *CHTenure* minus *CEOTenure*. *CHAge-CEOAge* is the age difference with *CHAge* minus *CEOAge*. *CHEducation-CEOEducation* is the difference in education level with *CHEducation* minus *CEOEducation*. *CHTitle>CEOTitle* is a dummy coded 1 if the chairperson has more title than CEO and 0, otherwise.

Control variables

Governance(Control) represents the control variables measuring corporate governance and board composition. Agency theory puts forward the importance of board of directors in monitoring the management (Fama, 1980). There are a number of internal governance mechanisms, such as board size, board independence and CEO duality, which have been

identified to be crucial factors to make sure that the management acts in the best interest of the shareholders (Shleifer and Vishny, 1997). Weisbach (1988) and Halebian and Rajagopalan (2006) find that CEO turnover decision is affected by board composition.

Board members are also responsible for providing advice and expertise in strategy formulation (Carpenter and Westphal, 2001; Judge and Zeithaml, 1992). *BoardSize* is the number of directors on board. *Independent Director* is the proportion of independent directors on board, which is used as a proxy for board independence (Cowen and Marcel, 2011). *Multiple Director* is the ratio of number of directors being the board members of more than one firm to total number of directors. *Female Director* is the percentage of female directors on board. *Average Age* is the mean age of directors and *Average Education* is the mean number of schooling of directors. Dalton et al. (1998) and Zhang and Rajagopalan (2004) show that CEO duality is related to turnover and hence we include *Dual*, which is a dummy coded 1 if the chairperson and CEO are of the same person and 0 otherwise in the model.

A better-governed firm should have an active board in performing the management monitoring function. We include three variables of meeting frequency as measures of board activity to assess the extent to which board members are active in performing various monitoring roles (Xie et al., 2003). *DirectorMeeting* is the number of directors' meetings, *AdvisorMeeting* is the number of advisors' meetings and *Shareholder Meeting* is the number of shareholders' meetings during the year. *Audit Quality* is a dummy coded 1 if the audit firm is one of the top-5 auditors according to total auditee assets within the industry group⁶ and 0, otherwise. Auditors perform a monitoring function to mitigate agency problems (moral hazard) (Jensen and Meckling, 1976) and hence higher quality auditors can improve corporate governance.

Firm(Control) represents the control variables for firm-specific characteristics. *Central SOE* is a dummy coded 1 if the firm is a SOE controlled by central government and 0 otherwise. *Local SOE* is a dummy coded 1 if the firm is a local SOE and 0 otherwise. In China, firms are either privately owned or state-owned. Further, state-owned firms (SOEs) can be divided into local SOEs (whose the controlling shareholders are local governments) and central SOEs (whose the controlling shareholders are central government). The other *Firm(Control)* are *ROA*, *Leverage*, *Firm Size* and *Firm Age*. *ROA* is returns on assets, which is a measure of profitability (Cowen and Marcel, 2011). Our measure of *Leverage* is debt to asset ratio. We use log of total assets as a measure of *Firm Size*. *Firm Age* is the number of years the firm established. Finally,

⁶The literature shows that industry specialization is a measure of audit quality. Following Francis et al. (2005), industry specialization is measured in terms of total audited assets in the industry group.

we include dummies for year and industry to control for changes in governance climate over time and across industry sectors.

3.3 Sample Description

Our data (financial statements, board information, ownership structure, special treatment announcements) are collected from the China Securities Markets and Accounting Research (CSMAR) database. The study covers a sample period of eight years from 2001 to 2008. We select firms from non-finance sector listed on the Shanghai Stock Exchange and Shenzhen Stock Exchange. In total, we have 7,978 firm-year observations for our analyses.

Table 1 reports the descriptive statistics of the variables.⁷ There are 673 observations with ST status. The number of turnovers for CEOs is higher, with 1,366 chairperson turnovers and 1,791 CEO turnovers. The chairperson and CEO turnover rates are 17.12% and 22.45%, respectively.⁸ Of the total 2,436 top management turnover, 1,070 CEOs are replaced. The mean year of chairpersons (*CHTenure*) staying in office is 3.88 years and that of CEO (*CEOTenure*) is 3.28 years. The chairpersons have an average age (*CHAge*) of 49.83 while the CEOs are younger with an average age of 45.94. The mean numbers of schooling for chairpersons and CEOs are 3.64 and 3.60, respectively. There are 4,766 chairpersons and 4,672 CEOs holding titles. The firm has a mean of about ten directors on the board. The ratios of independent directors (*Independent Director*), of directors with interlocking positions (*Multiple Director*) and of female directors (*Female Director*) are 0.30, 0.19 and 0.11, respectively. The mean age of directors (*Average Age*) is 48.45 and the mean number of schooling of directors (*Average Education*) is 3.54. A majority of firms (86.35%) do not have CEO duality (*Dual*). The mean frequencies of board meetings, advisor meetings and shareholder meeting are 8.07, 3.87 and 2.38, respectively. We find 2,146 firms selecting audit firms, which are industry expertise (*Audit Quality*). There are 1,579 and 4,052 central SOEs and local SOEs, respectively.

To examine H2, we need to differentiate voluntary and forced turnovers for our tests. Denis and Denis (1995) and Huson et al. (2004) document that it is a challenge to identify turnover type because it is unlikely for the firms to disclose the “true” reasons behind the

⁷We also calculate the bivariate correlations and variance inflation factor (VIF) values for the variables. To save space, they are not reported. The highest correlation coefficient and VIF value are 0.50 and 1.728, respectively, suggesting that our models do not suffer from multicollinearity problem.

⁸Our turnover rates for chairperson and CEO are lower than those reported by Firth et al. (2006), which is 40% and Chang and Wong (2009), which is 25.5%, but still higher than those documented for the US firms (12.7% in Denis and Denis (1995) and 9.3% in Huson et al. (2004)).

departures. Huson et al. (2001) and Hazarika et al. (2012) define forced turnovers for those cases when the CEOs are forced to leave due to policy difference or before the age of 60, or not because of retirement, death, personal health problem or taking another employment opportunity. However, such a method cannot be totally applicable in the Chinese data as a lot of top manager are forced to depart actually but use the excuse of personal health problem to save face.

Table1: Descriptive Statistics

	Dummy <u>Code = 1</u>	Dummy <u>Code = 0</u>	<u>Mean</u>	<u>Median</u>	<u>Max</u>	<u>Min</u>	<u>Standard Deviation</u>
<i>ST</i>	673 (8.44%)	7305 (91.56%)					
<i>CHTenure</i>			3.8838	3.0000	19.0000	1.0000	2.8521
<i>CHAge</i>			49.8300	50.0000	71.0000	26.0000	7.4445
<i>CHEducation</i>			3.6440	4.0000	9.0000	0.0000	2.4992
<i>CHTitle</i>	4766 (59.74%)	3212 (40.26%)					
<i>CEOTenure</i>			3.2825	3.0000	22.0000	1.0000	2.4804
<i>CEOAge</i>			45.9355	45.0000	75.0000	26.0000	6.7164
<i>CEOEducation</i>			3.5956	4.0000	9.0000	0.0000	2.4468
<i>CEOTitle</i>	4672 (58.56%)	3306 (41.44%)					
<i>BoardSize</i>			9.8444	9.0000	19.0000	5.0000	2.2197
<i>Independent Director</i>			0.3038	0.3333	0.6250	0.0000	0.1064
<i>Multiple Director</i>			0.1917	0.1429	0.8571	0.0000	0.1619
<i>Female Director</i>			0.1079	0.1111	0.7500	0.0000	0.1191
<i>Average Age</i>			48.4536	48.4286	65.8750	32.5000	4.3236
<i>Average Education</i>			3.5445	3.6000	8.4000	0.0000	1.6165
<i>Dual</i>	1089 (13.65%)	6889 (86.35%)					
<i>BoardMeeting</i>			8.0651	8.0000	36.0000	2.0000	3.3777
<i>AdvisorMeeting</i>			3.8710	4.0000	25.0000	1.0000	1.7441
<i>ShareholderMeeting</i>			2.3765	2.0000	14.0000	1.0000	1.2357
<i>Audit Quality</i>	2146 (26.90%)	5832 (73.10%)					
<i>Central SOE</i>	1579 (19.79%)	6399 (80.21%)					
<i>LocalSOE</i>	4052 (50.79%)	3926 (49.21%)					
<i>ROA</i>			0.0178	0.0321	2.5689	-3.9919	0.1915
<i>Leverage</i>			0.5110	0.4847	20.2467	0.0081	0.4939
<i>Firm Size</i>			21.3150	21.2076	27.8091	14.9375	1.0567
<i>FirmAge</i>			9.3921	9.0000	26.0000	1.0000	4.0965
<i>CHTurnover</i>	1366 (17.12%)	6612 (82.88%)					
<i>CEOTurnover</i>	1791 (22.45%)	6187 (77.55%)					
<i>CEOCHTurnover</i>	1070 (43.92%)	1366 (56.08%)					

Number of observations is 7,978. *CH* represents chairperson. *CEO* represents CEO. *Tenure*, *Age*, *Education*, *Average Age*, *Average Education*, *Firm Age* are in number of years. *Independent Director*, *Multiple Director* and *Female Director* are in proportion to total directors on board. *ROA* and *Leverage* are in percentages of total assets. *Firm Size* is in natural logarithmic form.

In the two studies on turnover in the Chinese market, Firth et al. (2006) use the stated reasons in the official corporate announcements made to the stock exchange and financial media to partition chairman turnovers into normal and forced⁹ while Chang and Wong (2009) employ the stated reasons from CSMAR to classify CEO turnovers into forced and non-forced.¹⁰ Practically speaking, both methods are very similar as CSMAR uses the same public data to code the dataset. However, the stated reason may not necessarily be the actual cause for departure. Firth et al. (2006, p. 1298) acknowledge that the stated reason of “voluntary resignation” may be a face saving device for a dismissed chairman. In addition, Akthaud-Day et al. (2006, p. 1129) also mention that firms may phrase dismissal in nice-sounding clichés (e.g., early retirement). Since there is no clear rule to determine the “genuine” reason for turnover, we do not attempt to make a classification of turnover type using the stated reasons provided by CSMAR in this study.¹¹

In addition, among many reasons, Firth et al. (2006) define forced turnovers as transferring back to the parent or controlling shareholder company before contract expiration. Such a classification is also problematic. In China, horizontal turnover of top management within corporate group or even between different firms for SOEs often means promotion to a more senior post in the government or a horizontal transfer to another SOE that need their help.¹² Thus, such a horizontal transfer mandated by the central or local governments who own majority control of SOEs has nothing to do with poor performance and should not be classified as forced

⁹Firth et al. (2006) define normal turnovers to include retirement, contract expiration, voluntary resignation, resignation for health reasons, and end of acting chairman role and forced turnovers to include undisclosed reason, transfer back to the parent or controlling shareholder company before contract expiration, change of company control, contract termination, personal reasons, improvement of corporate governance, and involvement in legal cases.

¹⁰Chang and Wong (2009) firstly exclude those turnovers with the stated reason as retirement, health, death, corporate governance reform, change in controlling shareholders, involvement in legal disputes and departure for chairman position from their sample of forced turnover. Then, based on five data sources (company annual reports, Infolink's China Economic News Database, Infolink's China's Listed Firms Database, China's Listed Firms Database and internet materials) to search for the destinations of departing CEOs to determine whether the nature of the new job. If the new job is worse (better) than the old one, the turnover is classified as a forced (non-forced) turnover.

¹¹Another reason why we do not follow the procedures of Firth et al. (2006) and Chang and Wong (2009) to use the stated reasons in CSMAR database to classify turnover type is because the forced turnover rates reported in their studies are too high. The forced turnover rates (relative to total turnovers) of chairperson is 47% in Firth et al. (2006) and of CEO is 30.98% in Chang and Wong (2009), which are also significantly higher than those documented for the US firms (13.3% in Denis and Denis (1995) and 18% in Huson et al. (2004)). Finally, we did run some analyses using the approach of Firth et al. (2006) and the findings for forced and voluntary turnovers are basically the same, which contradict to the intuition given by the two turnover types. We take this finding as an indication of poor methodology in identifying forced turnovers as mentioned in our paper.

¹²It is common to have high-level job rotations or switches among the SOEs. On January 16, 2012, with the approval of China Banking Regulatory Commission, extraordinary general meeting (EGM) and board meeting, the Agricultural Bank of China (ABC) and China Construction Bank (CCB) announced that ABC would appoint Jiang Chaoliang (previously as the president of China Development Bank) as chairperson and CCB would appoint Wang Hongzhang (previously as the Party member of the People's Bank of China) as chairperson.

turnovers. In this study, we make use of the incidence of reprimanding sanction and poor performance¹³ to divide the sample into voluntary turnovers and forced turnovers. When the firm is under reprimanding sanction or has poor performance, the top management in office should be dismissed. Therefore, the turnovers of the firms under reprimanding sanctions or have poor performance must be forced turnovers. Based on this logic, out of our total 7,978 firm-year observations, there are 6,975 observations, which are not under ST status and do not have poor performance, and hence we use these 6,975 observations for the test on voluntary turnovers. For the analysis of forced turnovers, we employ the 673 firms, which are under financial distress and ST status.

4. Results

4.1 Relationship between Management Demography and Financial Distress

For the first research question, we examine the types of quality of chairpersons and CEOs, which lead the firms to be under financial distress. The results are reported in Table 2.¹⁴ Of the four characteristics examined for chairpersons and CEOs, we find that *CHAge*, *CHTitle*, *CEOTenure* and *CEOEducation*¹⁵ are negatively related to *ST*. Their coefficients (-0.0196, -0.2763, -0.0609, -0.0685) are statistically significant ($p < 0.05$). These results suggest that the chairpersons who are younger in age and without title ownership and the CEOs with shorter tenure and low education level run the firms poorly and lead the firms to be under financial distress. For the TMT variables in Table 2, only the difference in ages is significant. The negative coefficient on *CHAge-CEOAge* implies that firms with younger chairpersons are more likely to be under financial distress. The findings support our H1 that management quality is related to incidence of reprimanding sanction.

Among the corporate governance variables, *Independent Director*, *Multiple Director*, *Average Age* and *Dual* are significantly related to *ST*. Board characteristics affect the strength of governance (Xie et al., 2003). We find a negative coefficient on *Independent Director*. We expect that the practice of interlocking directorates can mobilize the expertise of directors across firms and help firms to improve performance (Pettigrew, 1992; Schoorman et al., 1981). Our finding of a negative relation between the proportion of directors with multiple directorships (*Multiple Director*) and *ST* is consistent with our expectation. According to the organization learning and RBV theories, age can be a valuable intangible to enrich experience.

¹³We define firms with poor performance as firms have financial loss (negative return on assets and negative change in return on assets) and share price decrease (negative cumulative share return).

¹⁴For robustness purpose, we repeat the logit regression in Table 2 with the quality of chairperson and CEO in separate runs. The results are reported in Appendix 1.

¹⁵For robustness purpose, we also re-run the analyses using a dummy variable (coded 1 if the individual receives a 4-year university education and 0 otherwise) for *Education*. The results are qualitatively the same.

We find that the younger the mean age of the directors, the higher the likelihood that the firms would be under financial distress. Jensen and Meckling (1976) propose that CEO duality is a bad corporate governance practice.

In Table 2, the coefficient on *Dual* is positively significant, indicating that the probability of the firm being under reprimanding sanction is higher when the chairperson and the CEO are of the same person. We use the frequency of meetings to measure how active the board members are in performing the monitoring function (Xie et al., 2003). The frequency of advisor meetings (*Advisor Meeting*) is negatively related to *ST*, suggesting that the less frequent the board members meet in the advisor meetings, the higher the likelihood the firms to be under reprimanding sanction. Higher quality auditors can perform a better monitoring function to improve corporate governance. In Table 2, we find a negative relation between audit quality and incidence of reprimanding sanction (*ST*).

There are negative relations between *ST* with *Central SOE* and *Local SOE*, a result suggesting that privately-owned firms are more likely to be badly governed and perform poorly. Since the firms, which are under *ST* status are those firms, which have adverse financial conditions, a negative coefficient on *ROA* and a positive coefficient on *Leverage* are expected. In addition, we find that smaller firms (negative coefficient on *Firm Size*) and more mature firms (positive coefficient on *Firm Age*) are more likely to have adverse financial conditions. Collectively, these results demonstrate that the probability of financial distress is higher when the chairperson is younger and without professional certification title. The same is true when the CEO has shorter tenure and less education. In short, our overall results in Table 2 are consistent with our H1.

Table2: Logit Regression for Reprimanding Sanction

	<i>ST</i>			
	Coefficient	p-value	Coefficient	p-value
Intercept	12.2003	0.00	13.0807	0.00
<i>CHTenure</i>	-0.0111	0.63		
<i>CHAge</i>	-0.0196	0.02*		
<i>CHEducation</i>	-0.0360	0.16		
<i>CHTitle</i>	-0.2763	0.03*		
<i>CEOTenure</i>	-0.0609	0.02*		
<i>CEOAge</i>	0.0116	0.18		
<i>CEOEducation</i>	-0.0685	0.01**		
<i>CEOTitle</i>	0.0482	0.71		
<i>CHTenure-CEOTenure</i>			0.0129	0.48
<i>CHAge-CEOAge</i>			-0.0188	0.01**
<i>CHEducation-CEOEducation</i>			0.0064	0.76
<i>CHTitle>CEOTitle</i>			-0.0230	0.88
<i>BoardSize</i>	0.0245	0.31	0.0283	0.23
<i>Independent Director</i>	-2.2795	0.01**	-2.0879	0.02*
<i>Multiple Director</i>	-0.9208	0.01**	-0.7659	0.04*
<i>Female Director</i>	0.2712	0.51	0.0859	0.83
<i>Average Age</i>	-0.0322	0.01**	-0.0438	0.00**
<i>Average Education</i>	-0.0236	0.58	-0.1184	0.00**
<i>Dual</i>	0.3552	0.01**	0.2735	0.04*
<i>BoardMeeting</i>	0.0329	0.06	0.0403	0.01**
<i>AdvisorMeeting</i>	-0.0863	0.01**	-0.0824	0.01**
<i>ShareholderMeeting</i>	-0.0261	0.56	-0.0051	0.91
<i>Audit Quality</i>	-0.2745	0.04*	-0.2700	0.05*
<i>Central SOE</i>	-0.3621	0.02*	-0.3657	0.02*
<i>Local SOE</i>	-0.1739	0.14	-0.2917	0.01**
<i>ROA</i>	-10.8317	0.00**	-10.8827	0.00**
<i>Leverage</i>	2.4199	0.00**	2.4448	0.00**
<i>Firm Size</i>	-0.6270	0.00**	-0.6838	0.00**
<i>FirmAge</i>	0.0789	0.00**	0.0787	0.00**
Industry and Year Dummies				
Included				
LR Statistic	1773.65		1735.05	
p-value	0.00		0.00	

Notes: Number of observations is 7,978. *CH* represents chairperson. *CEO* represents CEO. *Tenure*, *Age*, *Education*, *Average Age*, *Average Education*, *Firm Age* are in number of years. *Independent Director*, *Multiple Director* and *Female Director* are in proportion to total directors on board. *ROA* and *Leverage* are in percentages of total assets. *Firm Size* is in natural logarithmic form. * and ** denote significance at 0.05 and 0.01 levels, respectively.

4.2 Relationship between Turnover, Financial Distress & Management Demography

For the second research issue (H2), we hypothesize that chairperson turnover¹⁶ is related to reprimanding sanction and management demography. Our results are reported in Table 3. Models 1 and 2 are the results for voluntary turnover and Models 3 and 4 are those for forced turnover. Some studies show that turnover is related to personal characteristics such as age (Huson et al., 2001; Kang and Shivdasani, 1995). In Models 1 and 2, we observe that chairperson turnover is related to age (*CHAge*), education level (*CHEducation*) and title ownership (*CHTitle*). The three coefficients (0.0318, -0.1050, -0.4834) are statistically significant ($p < 0.01$). These results suggest that there is a higher likelihood for chairpersons who are old, have low education level and no professional title to be replaced. For the characteristics of CEO, only *CEOTenure* and *CEOEducation* are significant. We find that chairpersons are more likely to be replaced when the CEOs have shorter tenure and higher education level. For the TMT variables, the differences in age (*CHAge-CEOAge*) and education level (*CHEducation-CEOEducation*) are positively and negatively significant, respectively ($p < 0.01$). For the forced turnover subsample in Models 3 and 4, we find a completely different result from Models 1 and 2. None of the chairperson characteristics are significant. For the characteristics of the CEO, only the coefficient on *CEOTenure*, which is -0.1403, remains its significance ($p < 0.01$). These results support our H2 that turnover is related to the characteristics of top management and incidence of reprimanding sanction.

Table3: Logit Regression for Voluntary and Forced Chairperson Turnover

	Voluntary <i>CHTurnover</i>				Forced <i>CHTurnover</i>			
	Model 1		Model 2		Model 3		Model 4	
	Coeff	p-value	Coeff	p-value	Coeff	p-value	Coeff	p-value
Intercept	-2.5563	0.00	-1.4500	0.12	2.7010	0.25	3.5519	0.12
<i>CHTenure</i>	0.0009	0.95			0.0683	0.10		
<i>CHAge</i>	0.0318	0.00**			0.0110	0.41		
<i>CHEducation</i>	-0.1050	0.00**			-0.0509	0.29		
<i>CHTitle</i>	-0.4834	0.00**			-0.3632	0.11		
<i>CEOTenure</i>	-0.0321	0.05*			-0.1403	0.00**		
<i>CEOAge</i>	0.0042	0.47			0.0175	0.26		
<i>CEOEducation</i>	0.0462	0.01**			-0.0297	0.46		

¹⁶In Table 3, we report the results for chairperson turnover only. However, similar analyses are also done for CEO turnover. The results are available upon request. For CEO turnover, *CEOAge* ($p < 0.01$) and *CEOTitle* ($p < 0.01$) are positively and negatively related to *CEOTurnover*, respectively. The coefficients on *Average Age* are negatively and significantly related to *CEOTurnover*, a finding suggesting that when the board members are younger in age, there is a higher likelihood for the CEO to be replaced. *ST*CEOAge* has a negative coefficient (-0.0386) and is significant ($p < 0.05$), which implies that younger (i.e., more inexperienced) CEOs are more likely to be removed when the firms are under special treatment status. As age is more likely to be positively related to voluntary turnover but not forced turnover (Huson et al., 2001), these findings suggest that we are able to capture a subsample of forced turnovers using the interaction terms for *ST* and various *Quality* variables.

<i>CEOTitle</i>	-0.0039	0.96			-0.1751	0.41		
<i>CHTenure-CEOTenure</i>			0.0050	0.68			0.0833	0.02*
<i>CHAge-CEOAge</i>			0.0144	0.00**			0.0007	0.95
<i>CHEducation-CEOEducation</i>			-0.0922	0.00**			-0.0004	0.99
<i>CHTitle>CEOTitle</i>			-0.1028	0.32			-0.3282	0.23
<i>BoardSize</i>	0.0206	0.21	0.0099	0.56	0.0214	0.61	0.0255	0.54
<i>Independent Director</i>	-1.5808	0.00**	-1.9295	0.00**	-2.2449	0.07	-2.0450	0.11
<i>Multiple Director</i>	0.1754	0.46	0.3447	0.14	-0.1194	0.87	0.0359	0.96
<i>Female Director</i>	-0.7869	0.01**	-0.8893	0.00**	-1.1131	0.10	-1.0175	0.13
<i>Average Age</i>	-0.0007	0.94	0.0037	0.68	-0.0128	0.59	-0.0100	0.66
<i>Average Education</i>	0.0629	0.03*	-0.0308	0.21	-0.0063	0.94	-0.1116	0.10
<i>Dual</i>	-0.7150	0.00**	-0.7266	0.00**	-0.3362	0.16	-0.4414	0.06
<i>BoardMeeting</i>	-0.0040	0.74	-0.0054	0.66	-0.0166	0.57	-0.0098	0.74
<i>AdvisorMeeting</i>	-0.0413	0.08	-0.0255	0.27	-0.0815	0.17	-0.0687	0.23
<i>ShareholderMeeting</i>	-0.0190	0.57	0.0051	0.88	0.0259	0.75	0.0396	0.62
<i>Audit Quality</i>	-0.1559	0.06	-0.1317	0.11	0.0975	0.69	0.0738	0.76
<i>Central SOE</i>	0.4739	0.00**	0.5002	0.00**	0.3500	0.20	0.2753	0.31
<i>Local SOE</i>	0.0425	0.65	0.0297	0.74	-0.0328	0.87	-0.0855	0.67
<i>ROA</i>	-3.9422	0.00**	-3.7121	0.00**	-0.1368	0.46	-0.1600	0.42
<i>Leverage</i>	0.1676	0.23	0.1545	0.32	-0.0414	0.62	-0.0514	0.55
<i>Firm Size</i>	-0.0437	0.30	-0.0393	0.34	-0.1041	0.30	-0.1187	0.23
<i>FirmAge</i>	0.0301	0.00**	0.0348	0.00**	-0.0321	0.24	-0.0305	0.25
Industry and Year Dummies	Included							
LR Statistic	370.94		287.45		70.36		56.44	
p-value	0.00		0.00		0.01		0.03	
Number of Observations	6975		6975		673		673	

Notes: *CH* represents chairperson. *CEO* represents CEO. *Tenure*, *Age*, *Education*, *Average Age*, *Average Education*, *Firm Age* are in number of years. *Independent Director*, *Multiple Director* and *Female Director* are in proportion to total directors on board. *ROA* and *Leverage* are in percentages of total assets. *Firm Size* is in natural logarithmic form. * and ** denote significance at 0.05 and 0.01 levels, respectively.

For the variables of *Governance(Control)* and *Firm(Control)*, some of them are significant in Models 1 and 2 but none of them is significant in Models 3 and 4. It is expected that the proportion of independent directors (*Independent Director*) should be positively associated with turnover. However, we find an opposite relation, a result, which is consistent with that of Dahya et al. (2002). *Female Director* is negatively related to *CHTurnover*, indicating that the higher the proportion of female directors on board, the less likely the chairperson would be replaced. *Dual* is negatively related to *CHTurnover*. The negative coefficient on *Dual* indicates that when the chairperson and CEO are of different persons, the chairperson is more likely to be replaced. Chang and Wong (2009) also find a negative relation between duality and CEO turnover in the sample of profit-making firms. For the three proxies of board activity, *Board Meeting*, *Advisor Meeting* and *Shareholder Meeting* as well as audit quality, none of the coefficient is significant.

We find *Central SOE* to be positively related to *CHTurnover*.¹⁷ In China, dismissals of CEOs in SOEs are in the hands of controlling shareholders (i.e., government). Chang and Wong

¹⁷In our analysis of *CEOTurnover* (results are available upon request), we find that *Local SOE* is negatively related to *CEOTurnover*.

(2009) argue that, owing to fiscal decentralization, local governments should place greater importance on economic performance than on achievement of social and political objectives and hence expect that firms owned by local government have stronger incentives than those owned by the central government to discipline poorly performing CEOs. Chang and Wong (2009) mainly focus on CEO turnovers. According to Article 114 of China's Company Law, the chairperson is the highest-ranked executive in Chinese firms and the CEO is the number-two person, second to the chairman (Firth et al., 2006). Therefore, our results of higher (lower) likelihood of chairperson (CEO) turnovers in central (local) SOEs suggest that SOEs tend to replace the chairperson, who is the highest-ranked executive, rather than the CEO. Our result of negative coefficients on *ROA* is consistent with that of Dalton and Kesner (1983) that poorly-performing firms have more top management turnovers. In addition, older firms have more top management turnovers.

For robustness test for Table 3, we use the total observations of 7,978 for analysis without classification of voluntary and forced turnovers. The results are reported in Appendix 2. We observe that when the firms are under reprimanding sanction, there is a higher likelihood of chairperson turnovers. The coefficients on *ST* are significantly and positively related to *CHTurnover* in three models ($p < 0.01$). For the characteristics of chairperson and CEO as well as TMT variables, we find similar results as in Models 1 and 2 in Table 3. As an additional test of the relation between turnover, ST status and quality of top management, we include interaction variables for *ST* and various *Quality* variables, *ST*CHTenure*, *ST*CHAge*, *ST*CHEducation* and *ST*CHTitle* for chairperson and *ST*CEOTenure*, *ST*CEOAge*, *ST*CEOEducation* and *ST*CEOTitle* for CEO. For Models 1 and 3 in Appendix 2, we find that there are significant relations between turnovers and various demographic characteristics. However, when *Quality* variables are interacted with *ST*, the coefficients on some characteristics of top management lose their significance and some show opposite signs. For instance, *ST*CHAge* and *ST*CHEducation* are not significant ($p > 0.10$). Furthermore, in Model 2, the coefficient on *ST*CHTitle* is positive (0.7450) and significant ($p < 0.05$), showing that a chairperson with professional qualification is more likely to be dismissed, a result which is different from that in Model 1. We find that chairperson turnover is positively related to incidence of ST status, chairperson's age and CEO's education; and negatively related to the education level and title ownership of chairperson and CEO's tenure. This finding raises an interesting question. If top management demography and incidence of financial distress jointly affect the probability of turnover, then what factors determine the turnover choice: chairperson versus CEO.

4.3 Scapegoating Effect of Forced Turnover

In the second research issue, we find that management demography and incidence of financial distress jointly affect the probability of chairperson turnover. Based on this result, we examine what factors determine the turnover choice: chairperson versus CEO. The results are reported in Table 4.¹⁸ In total, there are 2,436 observations of top management turnover, with 1,070 CEO turnovers. In Models 1 and 2, we use these 2,436 observations for analyses. For Models 3 and 4, we use only the subsample of firms with financial distress and top management turnovers. In total, there are 368 observations, with 110 CEO turnovers.

The results in Models 1 and 2 show that the choice of top management turnover (chairperson versus CEO) is significantly related to management demographic quality. All chairperson characteristics (*CHTenure*, *CHAge*, *CHEducation* and *CHTitle*) are significantly related to *CEOCHTurnover* ($p < 0.01$). *CHTenure* and *CHAge* have negative coefficients (-0.0514 and -0.0374). The two coefficients on *CHEducation* and *CHTitle* (0.0954 and 0.6212) are positive and statistically significant. These results suggest that CEOs are more likely than the chairpersons to be replaced when chairpersons are younger in age and more educated as well as have shorter tenure and professional qualification. For the CEO characteristics, only age (*CEOAge*) and education level (*CEOEducation*) are positively and negatively related to *CEOCHTurnover*, respectively. The coefficient on *CEOAge* (0.0290) is positive and statistically significant ($p < 0.01$). *CEOEducation* has a negative coefficient (-0.0473), which is significantly related to *CEOCHTurnover* ($p < 0.05$). These results indicate that CEOs are more likely to be replaced when they are older and less educated. For the TMT variables, the differences in tenure, age, education level and title are all significant. In addition, we also include the interaction terms for *ST* and various *Quality* variables. However, none of the interaction terms for *ST* and *Quality* variables of chairperson are significant. Only the coefficients on *ST*CEOTenure* (0.2068, $p < 0.05$) and *ST*CEOAge* (-0.0708, $p < 0.05$) are significantly positive and negative, respectively.

¹⁸For robustness purpose, we repeat the logit regression in Table 4 with the quality of chairperson and CEO in separate runs. The results are reported in Appendix 3.

Table 4: Logit Regression for the Choice of Turnover: Chairperson versus CEO

	<i>CEOCHTurnover</i>							
	Model 1		Model 2		Model 3		Model 4	
	Coeff	p-value	Coeff	p-value	Coeff	p-value	Coeff	p-value
Intercept	-1.2510	0.24	-2.0267	0.05	-5.4111	0.12	-6.7234	0.04
<i>ST</i>	0.4702	0.76	-0.4650	0.02*				
<i>CHTenure</i>	-0.0514	0.01**			-0.2473	0.00**		
<i>CHAge</i>	-0.0374	0.00**			0.0029	0.88		
<i>CHEducation</i>	0.0954	0.00**			0.1050	0.14		
<i>CHTitle</i>	0.6212	0.00**			0.3135	0.36		
<i>CEOTenure</i>	0.0335	0.14			0.3238	0.00**		
<i>CEOAge</i>	0.0290	0.00**			-0.0430	0.04*		
<i>CEOEducation</i>	-0.0473	0.04*			0.0494	0.46		
<i>CEOTitle</i>	-0.1020	0.38			-0.2156	0.51		
<i>CHTenure-CEOTenure</i>			-0.0376	0.03*			-0.2598	0.00**
<i>CHAge-CEOAge</i>			-0.0319	0.00**			0.0195	0.23
<i>CHEducation-CEOEducation</i>			0.0930	0.00**			0.0289	0.60
<i>CHTitle>CEOTitle</i>			0.2747	0.04*			0.3872	0.34
<i>ST*CHTenure</i>	-0.0142	0.87						
<i>ST*CHAge</i>	0.0327	0.18						
<i>ST*CHEducation</i>	0.0128	0.88						
<i>ST*CHTitle</i>	-0.5462	0.21						
<i>ST*CEOTenure</i>	0.2068	0.02*						
<i>ST*CEOAge</i>	-0.0708	0.02*						
<i>ST*CEOEducation</i>	0.1085	0.18						
<i>ST*CEOTitle</i>	0.1028	0.81						
<i>ST*(CHTenure-CEOTenure)</i>			-0.1005	0.20				
<i>ST*(CHAge-CEOAge)</i>			0.0424	0.03*				
<i>ST*(CHEducation-CEOEducation)</i>			-0.0799	0.26				
<i>ST*(CHTitle>CEOTitle)</i>			-0.5315	0.31				
<i>BoardSize</i>	-0.0114	0.58	-0.0078	0.70	-0.0378	0.56	-0.0346	0.61
<i>Independent Director</i>	1.1946	0.06	0.8354	0.07	4.3736	0.05*	3.7056	0.09
<i>Multiple Director</i>	-0.0862	0.77	-0.2083	0.47	0.8780	0.32	0.6983	0.41
<i>Female Director</i>	0.4831	0.21	0.5009	0.18	0.1663	0.87	0.2126	0.84
<i>Average Age</i>	-0.0187	0.09	-0.0129	0.22	0.0109	0.76	0.0017	0.96
<i>Average Education</i>	-0.0399	0.26	0.0396	0.20	-0.1203	0.23	-0.0209	0.81
<i>BoardMeeting</i>	0.0075	0.64	0.0040	0.79	-0.0228	0.64	-0.0212	0.66
<i>AdvisorMeeting</i>	-0.0141	0.61	-0.0192	0.48	-0.2379	0.00**	-0.2483	0.00**
<i>ShareholderMeeting</i>	0.0115	0.78	0.0074	0.85	-0.1240	0.31	-0.1089	0.37
<i>Audit Quality</i>	0.0203	0.85	-0.0162	0.88	-0.3084	0.45	-0.2688	0.48
<i>Central SOE</i>	-0.5944	0.00**	-0.5624	0.00**	-0.5691	0.17	-0.5441	0.19
<i>Local SOE</i>	-0.1799	0.10	-0.1865	0.09	-0.2192	0.49	-0.2278	0.46
<i>ROA</i>	0.2418	0.32	0.3093	0.19	-0.1363	0.49	-0.1222	0.52
<i>Leverage</i>	-0.1344	0.27	-0.1180	0.31	-0.0841	0.29	-0.0922	0.28
<i>Firm Size</i>	0.1294	0.01**	0.1425	0.00**	0.2782	0.09	0.2907	0.06
<i>FirmAge</i>	-0.0344	0.01**	-0.0344	0.00**	0.0141	0.74	0.0364	0.36
Industry and Year Dummies Included								
LR Statistic	264.26		216.23		64.86		54.60	
p-value	0.00		0.00		0.00		0.00	
Number of Observations	2436		2436		368		368	

Notes: *CH* represents chairperson. *CEO* represents CEO. *Tenure*, *Age*, *Education*, *Average Age*, *Average Education*, *Firm Age* are in number of years. *Independent Director*, *Multiple Director* and *Female Director* are in proportion to total directors on board. *ROA* and *Leverage* are in percentages of total assets. *Firm Size* is in natural logarithmic form. * and ** denote significance at 0.05 and 0.01 levels, respectively.

For Models 3 and 4, we restrict our analyses using firms with financial distress and top management turnovers to further explore the scapegoating effect. Comparing with the results in Models 1 and 2, fewer management characteristics are significant. *CHTenure* and *CEOTenure* exhibit opposite relations with *CEOCHTurnover*. *CHTenure* has a negative coefficient (-0.2473) while *CEOTenure* has a positive coefficient (0.3238), which are statistically significant ($p < 0.01$). In addition, the TMT variable, the difference in tenure between chairperson and CEO (*CHTenure-CEOTenure*) is also significant ($p < 0.01$). These findings suggest that tenure is an important factor determining which one should be replaced when the firms have difficult times. The longer the tenure of top management, the more accountable they should be and hence more likely to be replaced. These results indicate that certain top management's absolute and relative characteristics are clearly related to the forced turnover of CEO, supporting our scapegoating argument.

5. Discussion and Summary

Owing to the high concentration of ownership by controlling shareholders and the appointment of executives in SOEs by the central government, China has been documented to have serious entrenched management problem and expropriation of minority shareholders. However, we observe that there is a unique mandatory reporting requirement imposed by the CSRC to protect the interest of investors and to alert the investors about the adverse financial conditions of the firms. Therefore, we take advantage of this unique set of financially distressed firms in China to explore the effects of management and board characteristics on turnovers.

In this study, we examine the personal traits of top management, after controlling for different board governance structure and firm characteristics, which lead the firms for better or worse. The top management under examination includes the chairperson and the CEO, who are the two highest-ranking executives of the firm. We explore the relation between management characteristics, including age, tenure, education level and title (professional qualification) and incidence of reprimanding sanction, which is an indicator of poor performance. We find significant effects of top management demographic quality on incidence of reprimanding sanction and turnover, hence providing support to the upper echelons theory that the characteristics of top management do matter. Chairpersons who are younger in age and without professional title operate the firms poorly. Firms led by CEOs with shorter tenure and lower education level are more likely to be under reprimanding sanction. Besides, top

management turnovers are related to their demographic characteristics. Older chairpersons and CEOs with no professional titles have a higher likelihood of being replaced.

Using the unique data of reprimanding sanction to examine top management turnover, we provide evidence concerning the extent to which senior executives are to blame when firms are in distress, indicating some form of accountability expectation at the top management level. Our results are consistent with the scapegoating argument that management turnover is an important remedial step to provide a symbolic signal that a scapegoat should be detached from the firm. In particular, CEOs are more likely to be replaced when firms are under sanctions. These findings should have potential implications for the design of board governance structure and provide insights to regulators about the effectiveness and design of the current disciplinary, enforcement and prosecution systems.

Our study extends this literature by examining top management turnover for financially distressed firms. We control for board characteristics and governance and evaluate how top management demography can be related to financial distress and the subsequent turnovers. We believe that our study integrates the upper echelons and board governance literature and sheds insight on how management demography with various board characteristics can be related to turnovers for firms under financial distress.

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Appendix 1

Logit Regression for Reprimanding Sanction
(Chairperson and CEO in Separate Runs)

	<i>ST</i>			
	Coefficient	p-value	Coefficient	p-value
Intercept	12.5692	0.00	11.7665	0.00
<i>CHTenure</i>	-0.0200	0.39		
<i>CHAge</i>	-0.0180	0.01**		
<i>CHEducation</i>	-0.0474	0.04*		
<i>CHTitle</i>	-0.2443	0.03*		
<i>CEOTenure</i>			-0.0593	0.03*
<i>CEOAge</i>			0.0068	0.41
<i>CEOEducation</i>			-0.0835	0.00**
<i>CEOTitle</i>			-0.0806	0.49
<i>BoardSize</i>	0.0323	0.17	0.0302	0.20
<i>Independent Director</i>	-1.3424	0.03*	-1.8263	0.05*
<i>Multiple Director</i>	-0.7498	0.04*	-0.7920	0.03*
<i>Female Director</i>	0.1722	0.67	0.1972	0.63
<i>Average Age</i>	-0.0304	0.02*	-0.0381	0.00**
<i>Average Education</i>	-0.0842	0.04*	-0.0829	0.05*
<i>Dual</i>	0.3047	0.02*	0.3724	0.00**
<i>BoardMeeting</i>	0.0405	0.01**	0.0360	0.03*
<i>AdvisorMeeting</i>	-0.0644	0.05*	-0.0604	0.07*
<i>ShareholderMeeting</i>	-0.0050	0.91	0.0008	0.99
<i>Audit Quality</i>	-0.2690	0.04*	-0.2684	0.05*
<i>Central SOE</i>	-0.3710	0.02*	-0.3075	0.05*
<i>Local SOE</i>	-0.2435	0.04*	-0.2576	0.03*
<i>ROA</i>	-11.0421	0.00**	-10.9747	0.00**
<i>Leverage</i>	2.4743	0.00**	2.4762	0.00**
<i>Firm Size</i>	-0.6443	0.00**	-0.6760	0.00**
<i>FirmAge</i>	0.0887	0.00**	0.1010	0.00**
Industry and Year Dummies				
Included				
LR Statistic	1761.65		1764.60	
p-value	0.00		0.00	

Notes: Number of observations is 7,978. *CH* represents chairperson. *CEO* represents CEO. *Tenure*, *Age*, *Education*, *Average Age*, *Average Education*, *Firm Age* are in number of years. *Independent Director*, *Multiple Director* and *Female Director* are in proportion to total directors on board. *ROA* and *Leverage* are in percentages of total assets. *Firm Size* is in natural logarithmic form.

* and ** denote significance at 0.05 and 0.01 levels, respectively.

Appendix 2

LogitRegression for Chairperson Turnover

	<i>CHTurnover</i>							
	Model 1		Model 2		Model 3		Model 4	
	Coeff	p-value	Coeff	p-value	Coeff	p-value	Coeff	p-value
Intercept	-0.8902	0.28	-0.9100	0.27	-0.1091	0.89	-0.0646	0.94
<i>ST</i>	0.9288	0.00**	2.0324	0.09	0.9581	0.00**	0.8763	0.00**
<i>CHTenure</i>	0.0135	0.30	0.0144	0.29				
<i>CHAge</i>	0.0246	0.00**	0.0254	0.00**				
<i>CHEducation</i>	-0.0978	0.00**	-0.0956	0.00**				
<i>CHTitle</i>	-0.4721	0.00**	-0.5290	0.00**				
<i>CEOTenure</i>	-0.0392	0.01**	-0.0305	0.05*				
<i>CEOAge</i>	0.0023	0.66	0.0024	0.66				
<i>CEOEducation</i>	0.0324	0.05*	0.0351	0.04*				
<i>CEOTitle</i>	-0.0418	0.59	-0.0143	0.86				
<i>CHTenure-CEOTenure</i>					0.0128	0.24	0.0088	0.44
<i>CHAge-CEOAge</i>					0.0111	0.00**	0.0112	0.01**
<i>CHEducation-CEOEducation</i>					-0.0785	0.00**	-0.0825	0.00**
<i>CHTitle>CEOTitle</i>					-0.1238	0.18	-0.1490	0.12
<i>ST*CHTenure</i>			0.0123	0.82				
<i>ST*CHAge</i>			-0.0158	0.37				
<i>ST*CHEducation</i>			-0.0292	0.64				
<i>ST*CHTitle</i>			0.7450	0.02*				
<i>ST*CEOTenure</i>			-0.1406	0.04*				
<i>ST*CEOAge</i>			-0.0004	0.99				
<i>ST*CEOEducation</i>			-0.0404	0.46				
<i>ST*CEOTitle</i>			-0.2602	0.37				
<i>ST*(CHTenure-CEOTenure)</i>							0.0675	0.17
<i>ST*(CHAge-CEOAge)</i>							-0.0037	0.78
<i>ST*(CHEducation-CEOEducation)</i>							0.0521	0.21
<i>ST*(CHTitle>CEOTitle)</i>							0.3968	0.25
<i>BoardSize</i>	0.0084	0.58	0.0117	0.44	0.0110	0.47	0.0112	0.46
<i>Independent Director</i>	-2.4678	0.00**	-2.5128	0.00**	-2.0875	0.00**	-2.0943	0.00**
<i>Multiple Director</i>	0.0654	0.77	0.0693	0.75	0.2342	0.28	0.2276	0.29
<i>Female Director</i>	-0.7303	0.01**	-0.6911	0.01**	-0.8130	0.00**	-0.8096	0.00**
<i>Average Age</i>	-0.0015	0.85	-0.0016	0.85	-0.0029	0.72	-0.0033	0.68
<i>Average Education</i>	0.0351	0.18	0.0359	0.17	-0.0534	0.01**	-0.0556	0.01**
<i>Dual</i>	-0.6099	0.00**	-0.6085	0.00**	-0.6463	0.00**	-0.6466	0.00**
<i>BoardMeeting</i>	-0.0057	0.61	-0.0064	0.57	-0.0047	0.67	-0.0040	0.72
<i>AdvisorMeeting</i>	-0.0460	0.03*	-0.0454	0.03*	-0.0416	0.05*	-0.0413	0.05*
<i>ShareholderMeeting</i>	-0.0118	0.70	-0.0147	0.63	-0.0083	0.78	-0.0089	0.76
<i>Audit Quality</i>	-0.1231	0.11	-0.1263	0.10	-0.1081	0.16	-0.1103	0.15
<i>Central SOE</i>	0.4192	0.00**	0.4129	0.00**	0.4364	0.00**	0.4389	0.00**
<i>Local SOE</i>	-0.0040	0.96	-0.0110	0.89	-0.0217	0.78	-0.0236	0.76
<i>ROA</i>	-0.4314	0.02*	-0.4595	0.02*	-0.4705	0.02*	-0.4924	0.01**
<i>Leverage</i>	-0.0047	0.95	0.0209	0.76	-0.0098	0.91	-0.0002	1.00
<i>Firm Size</i>	-0.0753	0.05*	-0.0789	0.04*	-0.0665	0.07	-0.0669	0.07
<i>FirmAge</i>	0.0344	0.00**	0.0338	0.00**	0.0406	0.00**	0.0403	0.00**
Industry and Year Dummies Included								
LR Statistic	506.47		522.54		394.27		400.90	
p-value	0.00		0.00		0.00		0.00	
Number of Observations	7978		7978		7978		7978	

Notes: *CH* represents chairperson. *CEO* represents CEO. *Tenure*, *Age*, *Education*, *Average Age*, *Average Education*, *Firm Age* are in number of years. *Independent Director*, *Multiple Director* and *Female Director* are in proportion to total directors on board. *ROA* and *Leverage* are in percentages of total assets. *Firm Size* is in natural logarithmic form. * and ** denote significance at 0.05 and 0.01 levels, respectively.

Appendix 3

Logit Regression for the Choice of Turnover: Chairperson versus CEO
(Chairperson and CEO in Separate Runs)

	<i>CEOCHTurnover</i>			
	Model 1		Model 2	
	Coeff	p-value	Coeff	p-value
Intercept	-0.4160	0.70	-1.9375	0.06
<i>ST</i>	-1.7906	0.11	0.9084	0.51
<i>CHTenure</i>	-0.0401	0.03*		
<i>CHAge</i>	-0.0298	0.00**		
<i>CHEducation</i>	0.0870	0.00**		
<i>CHTitle</i>	0.5668	0.00**		
<i>CEOTenure</i>			0.0110	0.58
<i>CEOAge</i>			0.0155	0.03**
<i>CEOEducation</i>			-0.0434	0.05*
<i>CEOTitle</i>			0.0228	0.83
<i>ST*CHTenure</i>	0.0498	0.49		
<i>ST*CHAge</i>	0.0248	0.32		
<i>ST*CHEducation</i>	0.0456	0.56		
<i>ST*CHTitle</i>	-0.5380	0.22		
<i>ST*CEOTenure</i>			0.1681	0.04
<i>ST*CEOAge</i>			-0.0506	0.11
<i>ST*CEOEducation</i>			0.1358	0.06
<i>ST*CEOTitle</i>			0.0458	0.91
<i>BoardSize</i>	-0.0030	0.88	-0.0027	0.89
<i>Independent Director</i>	0.9796	0.11	0.9654	0.12
<i>Multiple Director</i>	-0.0255	0.93	-0.1351	0.63
<i>Female Director</i>	0.3917	0.31	0.4775	0.20
<i>Average Age</i>	-0.0125	0.25	-0.0154	0.15
<i>Average Education</i>	-0.0611	0.07	0.0377	0.25
<i>Dual</i>	0.8046	0.00**	0.8506	0.00**
<i>BoardMeeting</i>	0.0034	0.83	0.0034	0.82
<i>AdvisorMeeting</i>	-0.0060	0.83	-0.0040	0.88
<i>ShareholderMeeting</i>	0.0075	0.85	0.0435	0.27
<i>Audit Quality</i>	0.0056	0.96	-0.0484	0.65
<i>Central SOE</i>	-0.5412	0.00**	-0.5475	0.00**
<i>Local SOE</i>	-0.1397	0.20	-0.2181	0.04*
<i>ROA</i>	0.2085	0.40	0.2611	0.26
<i>Leverage</i>	-0.1070	0.39	-0.1118	0.32
<i>Firm Size</i>	0.1515	0.00**	0.1269	0.01**
<i>FirmAge</i>	-0.0333	0.01**	-0.0285	0.02*
Industry and Year Dummies Included				
LR Statistic	254.60		153.55	
p-value	0.00		0.00	
Number of Observations	2436		2436	

Notes: *CH* represents chairperson. *CEO* represents CEO. *Tenure*, *Age*, *Education*, *Average Age*, *Average Education*, *Firm Age* are in number of years. *Independent Director*, *Multiple Director* and *Female Director* are in proportion to total directors on board. *ROA* and *Leverage* are in percentages of total assets. *Firm Size* is in natural logarithmic form.

* and ** denote significance at 0.05 and 0.01 levels, respectively.