

What matters in executive compensation?
The Role of Internal Governance, Corporate Culture, and the Labor Market

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Abstract

Using a unique data set, we examine the relative importance of firm internal decision-making, corporate governance, corporate culture, and the labor market in explaining executive compensation. Our results suggest that the labor market and firm internal governance are the most important determinants. In particular, executives are compensated more and have a larger share of variable compensation if the firm's international activities make them highly exposed to the U.S. market, the highest paying and most liquid labor market for professional managers. In addition, pay is higher when boards are more inclined to favor shareholders at the expense of other stakeholders. We also find that executives receive a higher fraction of variable compensation in firms with dispersed ownership, especially if they take final decisions on strategic issues. We find no evidence that managerial entrenchment, as captured by social ties between executive and non-executive directors, can explain compensation. Finally, corporate culture appears to play only a minor role. Perhaps a bit surprisingly, in firms in which board members value achievement, executives receive lower pay.

The structure and the level of executive compensation differ enormously both across countries and across firms within the same country. In an international comparison, Murphy (1999) and Fernandes, Ferreira, Matos and Murphy (2008) show that not only U.S. CEOs are on average paid more than CEOs elsewhere, but also that they are paid differently.¹ A large part of the compensation of the highest paid U.S. CEOs appears to be in the form of incentive plans. Similar differences in executive compensation can be found across firms in the same country. For instance, Kaplan and Rauh (2007) point out the large dispersion in executive compensation in the U.S.

There exists an animated debate about the determinants of the level and the dispersion of executive compensation. Different explanations rely on the competitiveness of the executive labor market and the scarcity of managerial talent (Murphy and Zabochnik, 2004 and 2007; Frydman, 2005; Gabaix and Landier, 2008; Edmans, Gabaix and Landier, 2007), CEOs' power of setting their own pay in firms with disperse ownership and weak corporate governance (Bertrand and Mullainathan, 2001; Bebchuk and Fried, 2004), and culture and social norms regarding pay inequality and the socially acceptable level of executive compensation (Frydman and Saks, 2005; Piketty and Saez, 2006; Levy and Temin, 2007).

In this paper, we aim to shed light on the relative importance of these determinants of CEO compensation using a unique dataset of Swedish listed companies. The peculiarity of our data is that, besides having detailed demographic and ownership information, we survey executive and non-executive directors on decision-making processes and strategy choices within the firm and on their cultural values. Our data enable us to test whether differences in executive compensation across firms depend on the different roles and tasks that managers perform, as agency theory would predict, or on managerial entrenchment. In addition, since in Sweden board members are highly involved in setting executive compensation, we can ask

¹ Abowd and Bognanno (1995) and Abowd and Kaplan (1999) also point out large international differences in executive compensation.

whether board members' cultural values that are most likely to affect attitudes towards compensation levels and differentials are related to compensation. For instance, some directors may value highly personal achievement or exhibit tolerance for an asymmetric distribution of power and resources. We surmise that boards dominated by individuals who share these personal values should be more inclined to accept high executive compensation and rewards that are highly correlated with individual accomplishments thus leading to a higher proportion of variable pay.

Our data have other characteristics that make them highly appropriate to explore the most debated potential determinants of CEO compensation. First, although the average level of executive compensation is significantly lower in Sweden than in the U.S., differences in executive compensation are large: The CEO in the lowest percentile has a total pay that is over 100 times lower than the pay of the CEO in the highest percentile.

Second, our sample includes firms with highly heterogeneous ownership structure. According to Faccio and Lang (2002), Sweden has not only the highest percentage of widely held firms in continental Europe, but it makes the greatest use of control-enhancing mechanisms, such as dual class shares, pyramiding, and cross-holdings. Thus, not only can we ask whether the presence of large shareholders leads to lower CEO compensation, but also examine the effect of control-enhancing mechanisms that are believed to increase the principal shareholder's private benefits of control (Claessens et al, 2002).² Most importantly, large shareholders' involvement in managerial decisions and the role of the board are likely to differ a great deal in companies with so diverse ownership structure, making the environment ideal to explore the influence on executive compensation of the authority of the CEO in setting firm strategies, of monitoring and, of board entrenchment.

² Cronqvist and Nilsson (2003) show that this is the case also in Sweden.

Third, the sample includes firms with subsidiaries in a variety of countries as well as firms with only domestic production. Although the executive labor market is highly segmented, it is plausible that the executive directors of firms with large subsidiaries in a given country are more visible and familiar with its business environment and are thus more likely to receive offers to lead firms in this country. Theories stressing the importance of the managerial labor market for the level and structure of managerial compensation (e.g., Murphy and Zabojnik, 2007; Giannetti, 2007) would imply that executives who, because of U.S. operations, become visible in the U.S., the country with highest executive compensation, should have higher compensation than executives of companies that conduct international operations in other countries or that have mostly domestic production. We can thus test whether the managerial labor market plays any role in explaining differences in managerial compensation.

Finally, exploring the determinants of executive compensation within a country allows us to abstract from the effects of institutional differences and taxes while focusing on the relative importance of the executive labor market, corporate governance, and cultural values. An additional benefit of examining this issue in Sweden is that board composition and compensation are less subject to managerial control than in the U.S. In the U.S., board members are largely selected by the CEO.³ It is therefore plausible that boards are chosen to implement certain corporate policies and the compensation package that is most attractive to the CEO. As a consequence, the effects of variables measuring board characteristics, and cultural values in particular, are likely to be biased in compensation regressions due to reverse causality or correlation with unobserved measures of managerial power. In Sweden, unlike in the U.S., executives are not allowed to sit on the nominating committee, which represents the largest shareholders and institutional investors (Giannetti and Laeven, 2009). Thus, measures

³ Bebchuk and Fried (2004), amongst others, argue that one reason why pay levels in the U.S. are so high is because CEOs have too much power over their boards.

of board culture are arguably more exogenous in our compensation regressions than they would be for an U.S. sample.

Ultimately, we are aware that we cannot say for sure whether directors with certain characteristics determine the structure of compensation packages or are chosen to implement them. In addition, CEOs may choose companies with certain characteristics as well as shape corporate policies and compensation according to their preferences. Even with this consideration, we believe that our study provides unique information on the relation between the cultural values of board members and compensation.

Our results point to the labor market and corporate governance as the most important determinants of executive compensation. We find that executive compensation and the proportion of variable pay are higher when the CEO is more visible in the US markets. In addition, executives appear to obtain a lower fraction of variable compensation if controlling shareholders and board members –as opposed to the CEO– play an important role in setting firm strategy.

We also find that friendly boards (i.e., boards whose members are friends or have other social ties with the management) are not associated to higher compensation. Furthermore, in companies where board members value achievement, executive compensation is lower. This may indicate that board members oppose payments seemingly unrelated to performance if they value achievement. This finding also suggests that individuals who consider important to demonstrate competence may consider this an intrinsic motivation. In this case, extrinsic incentives under the form of higher (or more performance-related) pay may not only be considered unnecessary, but also damaging as extrinsic and intrinsic incentives have been shown to be often substitute (Gneezy and Rustichini, 2000).

Furthermore, to the extent that the emphasis on different cultural values varies across countries, our analysis can inform us on cross-country differences in executive compensation.

Since the U.S. culture is considered to put high emphasis on personal achievement and success (Schwartz, 2006), our findings imply that, *ceteris paribus*, culture should make the compensation of U.S. executives lower than for executives elsewhere in the world. Thus, culture and social norms are unlikely to be first order determinants of executive compensation.

This paper contributes to the executive compensation literature. The extant literature has explored the role of firm (e.g., firm size and performance) and managerial (e.g., job tenure and gender) characteristics.⁴ While we also consider these determinants, our main focus is the effect of internal decision-making and firm governance, corporate culture as well as the geographical distribution of firm activities.

Our paper is perhaps closest in spirit to Graham, Harvey and Puri (2008) who show that survey measures of CEOs' psychological traits and risk preferences are correlated with corporate outcomes, including compensation. We show that CEO characteristics are not the only ones that matter; the values and risk preferences of the board members responsible for setting CEO pay as well as the firm's objectives and executives' decision power are also important. In a recent paper, Bandiera, Guiso, Prat and Sandun (2009) explore the effect of family ownership on the policies for the promotion and remuneration of middle managers in Italy. Our paper consider the role of ownership, including family ownership, for top executives' pay, as opposed to middle managers.

The paper is also related to a growing literature that studies the effects of culture on economic outcomes and executive compensation in particular. Most of this literature focuses on macroeconomic outcomes (see Guiso, Sapienza, and Zingales (2006) for a survey). A notable exception is Bloom, Sadun and Van Reenen (2007) who show that differences in culture across firms are at least as large as cross-country cultural differences (Bloom, Sadun

⁴ See Murphy (1999) for a review.

and Van Reenen, 2007). This makes the cultural values of board members highly relevant for executive compensation.

Other papers consider the role of public attitudes and negative press, which may also be considered a manifestation of cultural values, on CEO compensation, but reach conflicting results. Kuhnen and Niessen (2009) show that negative public views of executive compensation expressed in local and national newspapers are associated with lower CEO compensation over time and across U.S. states. However, Core, Guay, and Larcker (2008) find little evidence that U.S. CEO compensation responds to negative press coverage, which should also be related to public views. Our paper introduces a novel proxy for corporate culture. While considering corporate culture (as opposed to state culture) is interesting in itself, our proxy has the advantage to be less likely to reflect transitory or permanent differences in executive labor market. Our results are broadly consistent with the findings of Core, Guay, and Larcker (2008).

The remainder of this paper is organized as follows. Section I describes the institutional environment; Section II introduces the data sources and the main proxies. Section III and Section IV present the results on the determinants of executive and non-executive directors' compensation, respectively. Section V concludes.

I Executive and Director Compensation in Sweden

Sweden has high standards of investor protection and, by continental European standards, a highly capitalized stock market (La Porta et al., 1998).⁵ As in the U.S., executive compensation is set by the board. The compensation committee decides upon executive compensation following guidelines it must submit to the Annual General Meeting (AGM) of

⁵ Sweden's stock market capitalization to GDP in 2002 was 85 percent, compared to 110 percent in the United States and 37 percent in Germany.

shareholders for approval. The compensation committee must consist of independent directors.

While Swedish boards are very similar to those in the U.S., they exhibit several peculiarities that make the study of compensation in Sweden particularly interesting. Unlike in the U.S. or the U.K., no more than one person on a Swedish board can be a senior manager, typically the CEO. The law also requires that the Chairman and CEO positions are separated. As in the U.S., Swedish boards have a nominating committee but this committee must have a majority of members who are not board members. No member of management may be represented on the nominating committee, nor should a director chair the nominating committee. Thus, a typical nominating committee may consist of the chairman of the board and several representatives of major shareholders (Giannetti and Laeven, 2009).

These features of Swedish board structure suggest that CEOs have less power over their boards than in the U.S. In addition, CEOs have less power to influence boards to award them higher pay through increases in director pay (“mutual back scratching”), as some have argued happens in the U.S. (e.g. Ryan and Wiggins, 2004 and Brick, Palmon and Wald, 2006). In Sweden, unlike in the U.S., the remuneration of directors is not decided by the compensation committee (Unger, 2006). Instead, the nominating committee, which contains no executive and only a minority of directors, puts forth a recommendation concerning director compensation which is voted on at the AGM.⁶ Furthermore, any shareholders may submit an alternative compensation proposal at the AGM. This suggests that our estimates are less likely to be biased because of reverse causality problems or correlation with unobservable measures of managerial control than they would be in a U.S. sample.

⁶ Anecdotal evidence suggests that shareholders and in particular institutional investors exercise a tight control over compensation. For instance, in April 2002, pension funds strongly opposed a three-year employee stock option scheme at Skandia, a large insurance company, because the scheme was judged too generous. As a consequence, the board withdrew the initial proposal and offered a less generous one-year scheme, accepted by the pension funds and a vast majority of the company’s shareholders.

Fernandes, Ferreira, Matos and Murphy (2008) report that in 2006 executive compensation in Sweden was lower than in the U.S., the U.K. and just below the Netherlands and Singapore. Swedish executive appeared better paid than executives in France, Germany and Hong Kong. In addition, incentive compensation is slightly above 25 percent of the overall compensation in the Nordic countries (including Sweden, Norway, Denmark and Finland). Although the average level of executive compensation in Sweden is slightly less than half in comparison to the U.S., as we document below, differences in executive compensation are large: The CEO in the lowest percentile has a total pay that is over 100 times lower than the pay of the CEO in the highest percentile. Differences in board fees are equally large: a board member can receive no compensation or SEK 3,000,000 (approximately, USD 400,000) as board fees. In addition, there exist large differences in the structure of contracts: While some firms offer CEOs no performance-pay, in over 10 percent of firms performance pay is more than half of the overall compensation.

A recent surveys of 1,000 individuals carried out by Demoskope during the 2009 financial crisis, in a period of intense and negative media coverage on executive pay, indicates that the public opinion in Sweden is largely in favor of performance-related pay for top managers. Almost 80 percent of the individuals surveyed considered high salaries to self-employed to be positive or highly positive (The Local, April 3, 2009).

II Data

A. Compensation

We hand-collect data on executive compensation for CEOs and, if available, Vice-CEOs (the equivalent of Presidents in a U.S. firm) of all listed companies from 2005 annual reports. We classify both CEOs and Vice-CEOs under the heading CEOs, because the distinction

between the two roles is not always clear and many companies only reports a CEO or a Vice-CEO.

We obtain information on salaries, bonuses, grants of equity, of stock options, other long-term incentive plans, pension plans, and perks. For option grants, we also collect information on strike prices, maturity, and granting date. If this information is not available, we assume that options have been granted on the first trading day of January at a strike price equal to the closing price of that trading day and that they have a maturity of three years.⁷ From annual reports, we also collect, where available, the fees of board members and of the chairman of the board.

Although the Swedish Industry and Commerce Stock Exchange Committee recommends companies to provide information on all the above items, firms disclose compensation to different extents. We obtain data on the compensation of 306 top executives (nearly 90 percent of them are CEOs, the remaining Vice-CEOs) in 273 of the 288 publicly-traded firms listed on the OMX (A&O list) and the NGM (Nordic Growth Market) in 2005 and the fee of board members (the chairman of the board) for 238 (180) firms.

Table 1 presents descriptive statistics on the various measures of compensation we use. Total compensation includes salaries, bonuses, equity and stock option grants, and other long-term incentive plans. Executives in the top decile earn more than 10 times of executives in the lowest decile. Total short-term compensation excludes long-term compensation, which as shown by the descriptive statistics is a minor component of the compensation for the executives with lowest pay. On average, variable compensation is slightly above 20 percent of the total compensation. Perks do not appear to be a significant component of compensation. Nearly 60 percent of the executives obtain retirement plans, whose taxation is deferred to retirement and that may be particularly important in Sweden because of the high income

⁷ In the empirical analysis we perform all the estimates both including and excluding option grants in our proxies for compensation, to make sure that these assumptions do not cause biases.

marginal tax rate. Slightly above 30 percent of the executives are granted options or equity during the year.

There exist a strong positive correlation between the level of executive compensation and board fees, even after controlling for firm size and industry. Perhaps surprisingly, the fee of board members are most often larger than the fee of the chairman of the board. This may depend on the fact that the latter is often a major shareholder or represents (is an employee of) a major shareholder.

B. Survey mechanism and design

We survey all executive and non-executive directors of Swedish listed companies in 2005 asking questions on their personal values, on the internal decision-making of the firm in which they serve, and on their personal ties with the CEO, the shareholders and other executive directors.

We measure cultural values using the 40-item Portrait Values Questionnaire (PVQ) developed by Schwartz (1992 and 1999) and Schwartz et al. (2001).⁸ The PVQ enables the researcher to infer cultural values by averaging the priorities of individuals. It confronts individuals with 40 different personal profiles (e.g., “It is important to him to be rich. He wants to have a lot of money and expensive things”). Respondents have to answer how much like them this person is on a scale from 1 to 6. Answers are then aggregated to obtain ten personal values, which according to Schwartz represent the motivating goals in human life. A higher score for a given cultural value signifies that individuals emphasize those traits more.

We consider not only directors' values regarding general aspects of life, but also the extent to which they stress the maximization of shareholder value as opposed to the welfare of

⁸ The Schwartz value survey has been replicated in many countries and Schwartz values have been shown to predict a variety of actions, ranging from voting behavior to altruistic behavior in experiments (Verplanken and Holland, 2002).

other firm's stakeholders. We gather information on these directors' views by prospecting some scenarios and asking what an hypothetical firm should do in those situations.

We also ask questions to evaluate the quality of corporate governance and internal decision-making. If a director seats on multiple boards at the time of the survey we select a firm at random and ask the director to answer the survey for that particular firm. To infer the objective of the firm, we ask whether in a recent important strategic decision, the interest of employers and other firm stakeholders were considered, besides the interests of shareholders.

In addition, to infer the authority of the CEO in making strategic decisions, we ask the directors to state their views on statements, such as “In our company, management usually makes final decisions on strategic issues”.

Similarly, we ask directors to declare the extent to which they agree with statements such as I am friend with most of outside (or executive) directors, with the CEO, or the major shareholders to evaluate the extent of social ties that may decrease the independence of the board.

Finally, the survey contains the following version of a standard question designed to measure risk attitudes (see, for instance, Dohmen, Falk, Hoffmann and Sunde, 2006): “Imagine you had won SEK 1,000,000 in a lottery. Almost immediately after you collect, you receive the following offer from a reputable bank: There is a chance to double the money within two years. It is equally possible that you could lose half of the money invested. Which amount of SEK 1,000,000 would you invest?: (1) 1'000'000 SEK, (2) 800,000 SEK , (3) 600,000 SEK, (4) 400,000 SEK , (5) 200,000 SEK, (6) 0 SEK.” Thus, risk-aversion increases with higher numeric responses to this question.

To carry out the survey, we used MM Partner, a database containing names of board members of all public and private firms in Sweden to identify the set of directors, CEOs and Vice CEOs of all publicly-traded firms in Sweden in 2005. Including Vice CEOs, these firms

have 468 CEOs and 1642 board members. We surveyed all CEOs and board members. The structure of the survey for CEO is similar to the one for board members, but we slightly adapt the questions regarding internal decision making to the different role performed by CEOs within the firm.

We were able to obtain addresses from an intermediary company for 424 CEOs/Vice CEOs and 1372 resident board members.⁹ The first survey was sent out on July 14, 2006. We followed it up with two reminders. The last survey response was received on November 11, 2006. The entire survey contained a total of 86 questions to board members and 82 to CEOs and Vice CEOs. To ensure that the Swedish questions reflected the meaning of the English questions, the English survey was first translated into Swedish and then reverse translated into English. In addition, recipient of the survey were guaranteed anonymity by mailing their responses to statistics Sweden, which matched the responses to data on personal and firm characteristics and removed all identifying information.

Overall, we received 502 responses (36.6 percent) from board members and 126 responses (29.7 percent) from CEOs and Vice CEOs.¹⁰ Some directors belong to the boards of several firms. On average, a non-executive director belongs to 1.88 boards. While the median board member belongs to only one board, over 10 percent of board members participate in 4 or more board of listed companies. If a board members seats in multiple boards, her answers, with the exception of those regarding decision-making within the firm, are attributed to all firms on whose board she seat.

We received at least one response from directors and CEOs of all but 36 (12.59 percent) of the 286 firms. The number of responses per firm with respondents varies from 1 to 8. All respondents filled out the entire value survey. Only 3 CEOs and 5 directors did not answer the risk question. The response rate is high compared to other surveys of top management teams.

⁹ To increase the response rate, the survey was mailed to the home addresses of each individual.

¹⁰ 32 of the CEO respondents are Vice CEOs, the rest are CEOs.

For example, Graham, Harvey and Puri (2008) report a response rate of 11 percent of CEOs, although their sample of CEOs is larger than ours. Overall, our sample size is comparable to that of other survey commonly used in the literature to evaluate management practices (see, for instance, Kaplan, Klebanov, and Sorensen, 2008).

Also, reassuringly, as shown in Table 1A in the Appendix, respondent and non-respondent directors have similar demographic characteristics.¹¹

C. Measuring corporate culture

Since board members represent a firm's owners and employees, their personal values may be thought to reflect the company's culture. If culture plays a role in explaining differences in executive compensation, one would expect that non-executive directors' basic beliefs and goals in life, in other words their personal values, affect executive compensation.

Cultural values (and the attitude associated with them) are listed in Table 2A in the Appendix. Here we focus the discussion on the values that are most relevant for executive compensation.¹² These are probably benevolence, achievement, and power. Those that think that benevolence is important aim to preserve and enhance the welfare of members of their own group. Executive and non executive directors are often considered to be linked by a tight network of social ties (see, for instance, Fracassi and Tate, 2009). Thus, non-executive directors who consider benevolence important may be willing to offer executives more generous compensation packages.

Individuals who consider power or achievement important equally focus on social esteem. The main difference is that achievement values emphasize actively demonstrating successful performance, whereas power values stress attaining or preserving a dominant

¹¹ The large coverage of listed companies that we are able to obtain eliminates concerns that our sample may be selected on the basis of firm characteristics.

¹² Adams, Licht and Sagiv (2009) also rely on the same survey and provide an in depth discussion of the 10 values.

position in terms of power and resources. The stress put on personal achievement or the tolerance of an asymmetric distribution of power and resources may increase the acceptance of high executive compensation and, in the case of achievement, of rewards that are highly correlated with individual accomplishments.

The cultural values we measure with our survey are well suited to capture attitudes towards executive compensation. For instance, American culture is considered to emphasize values such as ambition, success, daring, and competence, that is, personal achievement. In addition, unequal distribution of power, roles, and resources are considered more acceptable than, for instance, in Europe (Schwartz, 1999 and 2006). These cultural aspects have been considered to lead to high executive compensation in the U.S. and to moderate its growth in countries where more egalitarian values prevail (Piketty and Saez, 2006).¹³

We consider separately the cultural values of executive and non-executive directors. In particular, we focus on the cultural values of non-executive directors to explain executive compensation. We measure firm culture using the average of the personal values of the board members of the firm. As Table 1 shows, there exist considerable differences in cultural values across firms.

Measuring firm culture in this way may be problematic because not all board members answered the survey. The average number of responding non-executive directors in firms with respondents is 2.5, while the average number of board members per company is 8.03. Thus, if the values of the board members who responded are not correlated with those who did not, our proxies for firm culture are imprecise. More generally, if the variance of personal values between the board members of a given firm is the same as the variance between board members of different companies, our proxies for culture would only capture –with a noise– the average personal values of board members in Sweden.

¹³ Contrary to Western European culture, the U.S. culture tends to deemphasize in-group solidarity.

For these reasons, it is crucial to assess whether the personal values of the members of a given board are more congruent than the values of board members in different companies. In 70 percent of the companies for which we obtain the answers of at least two directors, the variance in the answers of the members of the same board is lower than the variance in the answers of all board members. This suggests that the personal values of members of the same board are more congruent than the personal values of board members of different companies and thus should capture at least some aspects of firm culture.

Notwithstanding this comforting evidence, the reader should keep in mind that incomplete coverage of directors introduces a measurement error in firm culture, thereby biasing our estimates against finding any results (cfr. Wooldridge, 2002, p. 73-76). Consequently, our positive results on the effect of firm culture can be downward-biased by measurement errors, while our negative results should be interpreted more cautiously as the lack of statistical significance may reflect the fact that our proxies are too noisy.

D. Internal Decision-Making and Corporate Governance

Existing theories (see, for instance, Burkart, Gromb and Panunzi, 1997) suggest that the role of the CEO may dramatically vary across firms depending on the extent of monitoring by the board and by larger shareholders. In particular, in some firms managers may take strategic decisions, while in others these are heavily influenced by the board or the majority shareholder. Whether the executive is the actual repository of decision-making power may have large importance on the structure and the level of executive compensation.

To evaluate who actually makes decisions in a firm, we ask directors to rate to what extent they agree in a scale from 1 (strongly agree) to 6 (strongly disagree) with the following statements: “In our company, management usually makes final decisions on strategic issues”;

“In our company, the board usually makes final decisions on strategic issues”; and “In our company, the major shareholder usually makes final decisions on strategic issues”.

We ask similar questions to the CEOs. We use their answers to verify whether the board members' responses actually capture firm practices. We find that they do. For instance, the correlation between the answers of the CEO and of the board members of a given firm to the question whether the major shareholder takes strategic decision is 30 percent and is significant at 1 percent level.

Therefore, on the basis of the board members' answers, we define a dummy variable (No decision power) that takes value 1 if board members agree or strongly agree that the major shareholders or the board make final decisions on strategic issues, and takes value zero otherwise. Interestingly, in slightly over 70 percent of the firms, the CEO does not appear to have a crucial role in taking crucial strategic decisions. We test whether managerial compensation is higher or more sensitive to performance when the management plays a crucial role in taking strategic decisions.

We also evaluate to what extent the board members are independent from the management. Although in Sweden executive directors are not allowed to the board, making all board members independent according to the U.S. regulatory definition, it is recognized in the literature that this definition of independence may be restrictive (Hwang and Kim, 2009). We define a board as friendly to the management if on average respondents at least slightly agree to the questions “I am friends with the CEO (most of the executive board members)”. Less than 25 percent of the board members can be classified as friendly with the CEO or other members of the management team.

Finally, we evaluate to what extent the board takes into consideration the interests of stakeholders, such as the firm's employees and the general society. This is again relevant for executive compensation because we expect pay to be linked to valuation to a larger extent in

firms that maximize shareholder value. We define two alternative proxies. The first captures board members' personal beliefs. We present board members with five stylized scenarios requiring to solve a trade off between shareholders interests and other stakeholders, which include consumers, workers, creditors, and the general society. We report in Appendix 3A the hypothetical scenarios which we present to board members. We define a firm to be shareholder-oriented if on average the respondents at least slightly agree in solving the conflict in favor of shareholders in all five scenarios. Interestingly, in only 1 percent of the sample firms, board members appear to be overwhelmingly in favor of shareholders.

The second proxy is constructed from the answer to the question whether in a recent important strategic decision of that firm the board discussed the impact of the decision on other stakeholders. Once again, we define firm to be shareholder-oriented if on average the respondents at least slightly disagree with the statement. We find that slightly less than half of the sample firms considered the impact of a recent strategic decision on stakeholders.

E. Ownership Structure

Our ownership data are from Värdepapperscentralen AB, the Central Security Registry. Swedish firms have relatively concentrated ownership: On average, the principal shareholders hold more than 30 percent of the votes. Additionally, principal shareholders often employ dual class shares, pyramiding, and cross-holdings to enhance their control rights. As a consequence, large differences can arise between the control rights and cash flow rights of the principal shareholder, leading to significant agency costs (Cronqvist and Nilsson, 2003).

Besides dual class shares, we take pyramiding and cross-holdings into account to determine the control rights of the principal shareholder, as is now common in the literature (e.g., Claessens, Djankov, Fan, and Lang, 2002; Faccio and Lang, 2002).

We classify a firm as having a controlling owner if the largest shareholder has direct and indirect voting rights that sum to 10 percent or more. Since 10 percent of voting rights is frequently sufficient to exert control, this cut-off is used extensively in the literature (e.g., La Porta, Lopez-de-Silanes, and Shleifer, 1999). If there are several chains of ownership, we sum the control rights across all of these chains. When multiple shareholders have over 10 percent of the votes, we pick the largest controlling owner.

In the empirical analysis, we focus on the following main proxies: First, we use the percentage of cash flow rights of the principal shareholder, which captures the incentives effects of ownership concentration. Shareholders with a larger percentage of cash flow rights should have stronger incentives to monitor managers and may also be directly involved in management. Because monitoring may substitute for pay, in firms with concentrated ownership compensation levels and performance pay may be lower.

Second, we use the wedge between control and cash flow rights of the principal shareholder, which captures the entrenchment effect of ownership concentration (Claessens, Djankov, Fan, and Lang, 2002). In companies with a high wedge between control and cash flow rights, the principal shareholder has strong incentives to extract private benefits. This may translate into higher pay not only for employees, as Cronqvist et al. (2009) argue, but also for executive and non-executive directors if these are to participate in the extraction of private benefits of control. There is no wedge between control and cash-flow rights for over half of the sample; the wedge can however be as large as 30 percent in companies with more pronounced separation.

Finally, we also consider the percentage of managerial ownership and hand-collect data on whether the CEO is the firm founder, defined as the individual who brought the firm public or a family member who replaced the founder from Fristedt and Sundqvist (2006). These characteristics are important for executive compensation. On the one hand, inside ownership

concentration provides incentives to maximize shareholder value and is a substitute for performance related pay;¹⁴ on the other hand, outside options are more limited for founders and especially family members, whose human capital is tied to the firm they own. Therefore, we would expect the structure of their pay to differ.

F. Firm international activity and executive labor market

We obtain data on the location of subsidiaries of Swedish listed companies from the 2006 edition of Orbis, a dataset distributed by Bureau Van Dijk. Orbis provides information on the subsidiaries, ownership and financial statements for listed and unlisted companies around the world. Besides the geographic location, we also obtain information on the amount of sales (in millions of U.S. dollars) that each of the subsidiaries originate.

We conjecture that executives are particularly exposed to the media and investors of the countries in which their company's subsidiaries generate a large amount of sales. Even though the empirical evidence on the differences in executive compensation strongly suggests that executive labor markets are segmented across national borders, executives are likely to become visible in the countries in which the foreign subsidiaries of their companies are more active. These executives should have higher likelihood to obtain job offers in these foreign countries. Thus, if the level and the structure of executive compensation are influenced by outside options and the labor market, we should observe that executives that are highly visible in countries with high executive compensation are paid more.

Since in the U.S. executive compensation is much larger than in the rest of the world, we hypothesize that the directors of companies that have subsidiaries with large amounts of sales

¹⁴ Note that, unsurprisingly, managerial ownership is much lower than the ownership of the principal shareholder. Not only the executives of listed companies often are professional managers, but also, when the principal shareholder is a family, several family members and foundations they control (and not a single individual) hold stocks in the firm. Their stockholdings are grouped to establish control as suggested by Sundin and Sundqvist (2001). However, the executive's stockholdings are to be considered her own individual stockholdings and are necessarily smaller.

in the U.S. should be paid more. In addition, we know that the higher compensation of U.S. executives originates from more incentive pay. We thus evaluate whether exposure to the U.S. market affects not only the level of compensation but also the proportion of variable compensation.

Table I shows that the level of subsidiaries' sales in the U.S. varies a lot across Swedish listed companies. Some listed companies have no subsidiaries in foreign countries (and therefore no sales from foreign subsidiaries), while others have a substantial amount of sales originating from subsidiaries in countries other than the U.S. These subsidiaries mostly aim to exploit low labor costs and are located primarily in Eastern Europe or in East Asia, where executive compensation is not higher than in Sweden. Thus, we do not expect visibility in these countries to have a positive effect on executives' outside options and, therefore, on the level and the structure of executive contracts.

G. CEO individual characteristics and social ties with board members

From Statistics Sweden we obtain detailed information on the demographic of the CEO, their wealth, their education, and their previous work experience. In particular, we know the employment history of the executives at intervals of three years since 1986. We can thus compute proxies for executive general skills using the number of previous jobs held by the executive or the number of industries in which the executive has experience.

Since we have similar information for the board members, we can compute proxies for social ties that rely on having attended the same college during the same period or having being employed in the same firm. These proxies complement the proxies for friendly boards based on the survey, which we introduced in Subsection D.II.

H. Other data sources

We complement the above sources with data on stock prices from SIX Trust and with accounting variables from Market Manager. Using these data we compute the return on assets (ROA) to proxy for firm profitability, the market to book ratio to proxy for firm growth opportunities, the logarithm of the firm's market capitalization, and the firm's return volatility using the standard deviation of the firm's biannual returns.

G. Correlations

It may be interesting to comment on the correlations between our proxies for firm internal decision making and corporate governance and ownership structure. The correlations are generally not significant. Among the few significant correlations, we highlight that family firms, firms with significant CEO ownership, and firms with friendly boards are less likely to have taken into account stakeholders in a recent strategic decision. The actual decision power of the CEO is unrelated to ownership structure. Firms with friendly boards as well as boards that monitor appear significantly more likely to have executives without decision power, suggesting that, when board members or the CEO are in charge of strategic decision, they may choose a friend as a CEO.

III Results on Executive Compensation

A. Executive pay level

In Table 2, we relate an executive's total compensation to the cultural values of the board members of the firm in which she is employed. To begin with, we include only controls for firm characteristics that are well known to affect executive compensation, such as firm size (proxied by the logarithm of stock market capitalization), firm profitability, and firm growth opportunities (see, for instance, Core, Holthausen and Larcker, 1999 and Smith and Watson, 1992).

Consistently with previous empirical evidence, firm size is always positively and significantly related to total compensation. Among the other variables, only board members' emphasis on achievement appears to have a statistically significant effect on compensation. In particular, executives seem to receive lower compensation if their board members value achievement. The effect is not only statistically, but also economically significant: If the emphasis that board members put on achievement increases by one standard deviation, the total compensation of an executive decreases by almost 10 (over 15) percent of its mean value if we consider the most (least) conservative estimate in column 5 (7).

These results may indicate that boards that value achievement oppose large payments seemingly unrelated to performance. Board members may also consider extrinsic incentives under the form of higher (or more performance-related) pay unnecessary or even damaging as extrinsic and intrinsic incentives have been shown to be often substitute (Gneezy and Rustichini, 2000). Interesting, since the U.S. culture is considered to put high emphasis on personal achievement (Schwartz, 2006), our findings imply that, if anything, culture should make the compensation of U.S. executives lower than for the executives elsewhere in the world.

In column 7, we include all cultural traits together. We find that board members who value conformity and that therefore do not want to violate social expectations and norms offer lower compensation. A one-standard deviation increase in the desire to conform of board members decreases executive compensation by 12 percent of its mean value. This indicates that board members who wish to conform may oppose large compensation packages and is consistent with the notion that social norms may affect executive compensation. The extent to which board members value conformity appears to have a statistically significant effect only if we control for all other cultural values.

None of the other cultural values, besides achievement and conformity, appear to have a significant effect on compensation. For instance, it does not seem that an emphasis of board members on power, which implies high tolerance for an asymmetric distribution of resources and power, has any relation with compensation. Similarly, we explore whether a tendency of the board towards egalitarian values is related to the level of compensation in two ways. First, we exploit the answer to the question “He wants everyone to be treated justly, even people he doesn’t know. It is important to him to protect the weak in society”. Individuals who recognize themselves in this profile should have more egalitarian values and may be against large differences in compensation. Second, we explore the effect of ‘universalism’. Individuals who emphasize these cultural values are considered to aim to understand, protect, and appreciate all people and may thus be more averse to large differences in compensation. We find no evidence of this. Estimates also suggest that board member risk aversion does not affect the level of executive pay.¹⁵

Overall, the values of board members as well as their risk attitudes not only exhibit small statistical significance, but also explain a small fraction of the variance of the model. For instance, in column 6 of Table 2, over 86 percent of the variance of the model is explained by firm market capitalization. The cultural values jointly explain around 13 percent.

In Table 3, we include variables capturing ownership structure and firm level corporate governance. Estimates in column 1 show that, if the principal shareholder has a larger proportion of cash flow rights, executive compensation is lower. The effect is sizable from an economic point of view: A one standard deviation change in the percentage of cash flow rights held by the principal shareholder decreases executive compensation by approximately 15 percent of its mean. This suggests that ownership concentration favors monitoring by the

¹⁵ Note that here we are using 9 of the 10 Schwartz cultural values. For evaluating board risk aversion, we present results based on board members’ answer to the question that directly evaluates risk taking. Results would be qualitatively similar if we used the Schwartz’ cultural value measuring the extent to which an individual values security.

principal shareholders and that higher monitoring may substitute for incentive pay. At least in some specifications, a larger wedge between control and cash flow rights for the principal shareholders seems to bring higher compensation (a one-standard-deviation change in the wedge increases executive compensation by approximately 15 percent of its mean). This may suggest that in these companies controlling shareholders extract more private benefit of control and, being less motivated by cash flows, are willing to offer larger compensation packages to managers.

We explore whether the firm's internal governance matters beyond ownership structure. In column 2 of Table 3, we find no additional effect of management power in making strategic decisions on the level of compensation. In an unreported specification, we find that also the extent of board monitoring is irrelevant. Column 3 shows that firms in which founders or family members are involved in management pay less their executives, even after controlling for ownership. Interestingly, an even more important role seems to be played by what board members believe that the objective of the firm should be. A board more oriented to maximize shareholder value is associated with significantly higher compensation.¹⁶ We find no association between the presence of individuals on the board who are personal friends of the management and compensation. This is the case also if we use proxies for the social ties between CEO and board members, such as having the same birthplace or having attended the same school.

Finally, we include our proxy for the executive exposure the U.S. market, the logarithm of U.S. based subsidiaries sales. Consistent with the hypothesis that potential outside options matter, we find a positive effect of the logarithm of U.S. sales on compensation. This is unlikely to capture the size and the complexity of the firm as more sales in subsidiaries that are not located in the U.S. appear to be unrelated to compensation. The effect of our proxy

¹⁶ The dummy capturing whether other stakeholders were considered in recent discussion about strategic decisions does not appear statistically significant, suggesting that these issues may often be discussed in the board room because of laws and regulations.

capturing how visible an executive is to the U.S. market is also large from an economic point of view. A one standard deviation increase in the logarithm of U.S. sales appears to increase executive compensation by nearly 25 percent at its mean.

In Table 4, we explore the robustness of the above results to the inclusion of additional controls on firm and especially executive characteristics and a different definition of total pay. First, since our data include pay levels for CEOs and a few Vice-CEOs, we include a dummy variable that takes value 1 if the observation refers to a CEO. As we would expect, CEOs have higher compensation than Vice-CEOs, although the dummy variable is not statistically significant at conventional levels (this is probably due to the fact that the dummy variable is equal to 1 for nearly 90 percent of the sample and that the distinction between CEOs and Vice-CEOs is not clear). Although the coefficient of the percentage of cash flow rights of the principal shareholders loses significance, all our results are qualitatively invariant.

In column 2, we control for the percentage of the capital directly owned by the CEO. This is likely to be larger for individuals who are family members. As one would expect, the higher the shareholdings of the CEO the lower is executive pay. However, the effect is once again not significant at conventional level; this is probably due to the fact that this effect is already captured by the founder or family dummy.

In column 3, we include some demographic characteristics and the cultural values of the executive as controls. Here, our sample is severely reduced by whether the executive answered the questionnaire. Interestingly, we find that executives that value power receive higher compensation. Whether the executives value achievement or other cultural values of the executive do not appear to matter in specifications that we do not report for brevity. Although our sample is greatly reduced, the most of our results relating firm characteristics to CEO compensation appear robust. The only noteworthy difference is that the extent to which board members value achievement loses statistical significance. Somewhat surprisingly,

female executives that in this subsample are fewer than 5 percent appear better paid. The remaining executive demographic characteristics, including age and the number of previous employers of the executive, appear to have no effect on compensation.

In column 4, we explore whether our results on board culture may be biased by the number of respondents. For instance, firms for which a larger number of board members answered our questionnaire may differ from the rest along a number of unobservable dimensions. Our results are unaffected. Moreover, the number of board members answering the questionnaire is not related to compensation.

In column 5, we consider that the value of stock options new awards, which so far was included in our measure of compensation, is imprecisely calculated in some instances. Therefore, we rerun our regressions using a measure of total pay that does not include options. Our estimates appear invariant.

Finally, in column 6, we control for firm profit volatility. This variable does not seem to affect executive compensation nor its inclusion modifies our previous findings.

The strongest and most robust finding emerging from the previous analysis is that firms whose U.S. subsidiaries originate a larger amount of sales offer more generous compensation packages to their executives, possibly because, being visible in the U.S., their executive have stronger outside options. Overall, this suggests that the executive labor market has an important role in explaining differences in pay levels.

B. The proportion of variable pay

The structure of compensation is at least as important as its level. For this reason, in Table 5, we relate the proportion of variable compensation to firm characteristics, including

ownership structure, board cultural values, and the proxies capturing an executive's visibility in foreign labor markets.¹⁷

It appears that larger firms not only pay their executives more but also offer a larger proportion of variable pay. Other firm characteristics, including the values of board members and the firm's ownership structure, seem to be unrelated to the proportion of variable compensation. The lack of importance of ownership concentration contrasts with the Italian empirical evidence for middle managers showing that principal shareholders with large private benefit of control are less likely to offer performance-sensitive managerial contracts (Bandiera, Guiso, Prat and Sadun, 2009). Only in column 11, we find some evidence that, the larger is the wedge between control and cash flow rights of the controlling shareholder, the lower is the proportion of variable pay suggesting that controlling owners with strong incentives to extract private benefits of control have no incentive to ask executives to maximize cash flow rights. Also, unsurprisingly, high CEO equity ownership appears to be a substitute for variable pay.

The role of CEOs in taking strategic decisions, rather than ownership structure, appear to matter for managerial contracts. We consistently find that executives are offered a lower proportion of variable pay if the board or the principal shareholder have the final say on strategic decisions.

Furthermore, our estimates once again indicate that the managerial labor market may be the main driver of differences in the structure as well as in the level of executive compensation. The proportion of variable pay is positively affected by the volume of sales generated by U.S. based subsidiaries, but not by that of subsidiaries in other countries, thus suggesting that an higher likelihood of receiving offers from U.S. companies affects not only the level but also the structure of the managerial contract. This is consistent, for instance, with

¹⁷ We estimate the equations using ordinary least squares, instead of using a tobit model, because in presence of non-normal residuals only the former are consistent. Results would be qualitatively similar with a Tobit estimator.

Giannetti's (2009) model. The effect of our proxy for an executive visibility in the U.S. market is also economically large: A one standard deviation increase in the logarithm sales originated by U.S. subsidiaries results in an increase in the proportion of variable pay by over 20 percent from its mean.

In columns 7 we include some executive characteristics as explanatory variables. In particular, we include a measure of the executive risk aversion based on our survey question. Similarly to Graham, Harvey and Puri (2008) as well as Bandiera, Guiso, Prat and Sadun (2009), who also use survey based measure of managerial risk aversion, and consistently with economic theory (Holmström, 1979), we find that more risk averse managers have compensations packages that include a lower proportion of variable pay. Once we control for the executive's risk propensity, also the risk propensity of board members seem to be related to the proportion of variable pay, which is lower, the more risk averse board members are.

C. Other features of executive compensation

In Table 6, we consider other features of executive compensation and relate them to our proxies for firm culture, governance, and executive labor market. We first consider the value of perks received by executives. Also this component of compensation appears to be larger in larger companies. Board culture also seems to have some explanatory power. More tolerant and understanding board members, as measured by a larger emphasis on the universalism cultural value, appear to consistently allow executives to enjoy more perks. We also find some, weaker, evidence that boards that are more inclined to accept customs and ideas are associated to firms where executives enjoy more perks. These findings may indicate that some boards choose to adopt a path a least resistance and just passively comply with the preferences of executive directors. Firms seem to provide less perks when their board members are more concerned with violating social expectations and norms (i.e., value conformity).

Social ties between executive and non-executive directors do not appear to be associated to the level of perks in the same way as they are not associated to the level of executive compensation.

Interestingly, principal shareholders that are expected to extract more private benefits of control because of a high wedge between control and cash flow rights appear to offer more perks to their executives.

In column 5 and 6 of Table 6, we consider the probability that an executive receives pension plans or stock options, respectively. Retirement pay and perks appear to have similar determinants as more tolerant and understanding board members are more likely to agree to retirement pay. Retirement pay may be more compatible with social conventions and norms as board members that value conformity are more likely to offer it.

In addition, executives are more likely to obtain a retirement plan if they play an important role in strategic decisions. Consistently with the notion that rich contributions to executive pension plans do not affect incentives and promote performance, companies with higher growth opportunities and more severe retention problems, created by the visibility of the executive in the U.S. labor market, are less likely to offer retirement plans.

Options are instead more likely to be chosen by companies with large sales in the U.S. and with lower ownership concentration. Interestingly, firms with boards that find acceptable a more asymmetric distribution of power appear less likely to award options.

IV. The Compensation of Non-Executive Directors

Since we note a strong positive correlation between the levels of compensation of executive and non-executive directors, in Table 7, we relate board fees to the factors that we have explored as potentially important for executive compensation. We consider the fee of members of the board as well as the fee of the board chairman.

Not surprisingly, executive and non-executive compensation have similar determinants. Board fees are larger in larger companies as well as in firms that generate larger amount of sales through their U.S. subsidiaries. Board members that value achievement seem to earn lower fees as the executives in their companies do. Interesting, if the CEO values challenge and novelty (i.e., stimulation), board members tend to be more highly paid. There is also some evidence that board member that value stimulation earn larger fees. This may indicate that non-executive directors are better remunerated if executives values the challenges and new ideas of board members. However, we find no evidence that boards whose members agree or strongly agree to the statement "I am often asked by the CEO to provide advice and counsel" obtain larger fees. Board fees are also not associated to board perceived power of affecting corporate decisions.

Also, there is some, although not always significant at conventional levels, evidence that board fees are lower in firms with concentrated ownership and larger in firms in which the principal shareholder has a large wedge between control and cash flow rights. This may suggest that board fees are used to share control benefits. We find no evidence, however, that board whose members are friends with the management or the major shareholder receive higher fees.

V. Conclusions

We surveyed all executive and non-executive directors of Swedish listed companies to obtain information on the cultural values of board members, of the CEOs, and information on firms' internal decision making and objectives. We relate board members' survey answers as well as information on firm ownership structure and other firm and executive characteristics to executive and non-executive compensation.

We show that the role of CEOs in taking strategic decisions is related to the structure of the managerial contract. In particular, CEO with more decision power obtain more variable compensation. Furthermore, the extent to which board members are willing to sacrifice the welfare of firm stakeholders in order to maximize shareholder value is positively associated to the level of pay.

We also find that both the level of pay and the proportion of variable compensation are higher if the firm's international activities make the CEO highly exposed to the U.S., the highest paying and most liquid market for professional managers. In contrast, social ties between members of the board and management do not explain differences in managerial compensation, suggesting that these are not driven by managerial entrenchment.

Finally, differences in corporate culture, proxied by the cultural values of board members, appear to have limited role. Interesting, boards that value achievement are associated to lower executive compensation.

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Table 1
Descriptive Statistics

Total compensation includes salaries, bonuses, equity and stock option grants, and other long-term incentive plans. Short-term compensation includes salaries and bonuses. Variable compensation is the proportion of bonuses, equity and stock option grants in the total compensation. Perks is the value of perks, such as housing, corporate planes or cars, granted to the CEO. Retirement plan is a dummy variable that takes value 1 if the CEO is granted a retirement plan from the company and zero otherwise. Options is a dummy variable that takes value equal to 1 if the CEO is granted equity or options and value zero otherwise. Board member fee is the fee received by board members. Board chairman fee is the average fee received by the chairman of the board. The personal values (achievement, universalism, benevolence, conformity, tradition, hedonism, stimulation, self-direction, power and risk) are calculated as the average of the personal values of the responding board members for each firm. The variables range from 2 to 6 and a higher number means more emphasis on that personal value. Description of the personal values can be found in Table 2A. Risk is a measure of risk of the average risk aversion of the responding board members. No decision power is a dummy that takes value equal to 1 if on average the board members at least slightly agree that the final decision on strategic issues is made by the board or the majority shareholder, but not by the manager. Friendly board is a dummy variable that takes value 1 if on average the board members at least slightly agree that they are fired with the CEO or other executive directors. Shareholder orientation-value is a dummy that takes value equal to 1 if considering some hypothetical scenarios, described in Appendix 3A board members always state that they at least slightly agree in solving the trade off in favor of shareholders. Shareholder orientation-actual is a dummy variable that takes value equal to 1 if in a recent strategic decision board members did not consider the impact on stakeholders. Cash flow right max is the percentage of cash flow rights of the principal shareholder. Wedgemax is the difference between control rights and cash flow rights of the principal shareholder. CEO ownership is the percentage of shares held by the CEO. Founder or Family is a dummy that takes value equal to 1 if the CEO is the founder or a family member of the principal shareholder. US sales are the sales originated from US subsidiaries in million. Other sales are the sales originated from foreign subsidiaries other than US subsidiaries in million. ROA is the firm's return on assets. Growth opportunities is the firm's market to book ratio. Log market capitalization is the logarithm of the firm market capitalization. Volatility is the standard deviation of the firm's biannual returns from 1997 to 2007. CEO achievement, CEO risk, and CEO power are the corresponding personal values of the CEO. Male is a dummy that takes value equal to 1 if the CEO is a male. Age is the CEO's age. No previous employers is the number of previous employers of the CEO starting from 1986.

Variable	Mean	Standard Deviation	10%	Median	90%	N
Compensation						
Total compensation	4055248	4401000	830540	2668500	8827000	306
Short-term compensation	3595978	3469214	800000	2401500	7594858	306
Variable compensation	0.21355	0.232639	0	0.167129	0.557677	305
Perks	61315.79	179077.5	0	0	144000	333
Retirement plan	0.594595	0.491709	0	1	1	333
Options	0.318318	0.466525	0	0	1	333
Board member fee	375545.2	404617.2	76000	250000	900000	238
Board chairman fee	149787.8	97624.3	50000	125000	300000	180
Board culture						
Achievement	3.775663	0.638239	3	3.75	4.5	289
Universalism	4.119723	0.565156	3.5	4.166667	4.833333	289
Benevolence	4.328576	0.55856	3.75	4.375	5	289
Conformity	3.441321	0.707813	2.5	3.5	4.25	289
Tradition	2.459775	0.464744	2	2.5	3	289
Hedonism	3.707036	0.849782	2.5	3.666667	4.833333	289
Stimulation	3.658016	0.701095	2.666667	3.666667	4.333333	289
Self-direction	4.730825	0.509919	4.25	4.75	5.375	289
Power	3.33391	0.555295	2.666667	3.333333	4	289
Risk	4.40625	1.052571	3	4.5	6	288
Equal treatment for everyone	4.42	0.77	3.5	4.5	5	288
Internal decision-making and corporate governance						
No decision power	0.71	0.45	0	1	1	289

Monitoring board	0.12	0.33	0	0	1	334
Friendly board	0.24	0.43	0	0	1	334
Shareholder orientation-value	0.01	0.08	0	0	0	334
Shareholder orientation-actual	0.51	0.5	0	1	1	334
Ownership structure						
Cash flow right max	31.7	20.57	9.93	27.15	64.02	316
Wedgemax	9.17	12.58	0	0	29.36	316
CEO ownship	3	1.1	0	0	6	333
Founder or family	0.26	0.44	0	0	1	334
Labor market proxies						
US sales	91393.72	448187.7	0	0	23000	333
Other foreign sales	2944280	1.37E+07	0	78480	2757440	333
Firm characteristics						
ROA	0.25	0.44	0	0.08	0.75	333
Growth opportunities	2.3	2.31	0.71	1.63	4.69	280
Log market capitalization	20.79	2.7	18.29	20.56	24.08	289
Volatility	0.4	0.29	0.17	0.33	0.74	286
Executive characteristics						
CEO achievement	4.01	0.88	3	4	5	135
CEO risk	2.7	1.5	1	3	5	132
CEO power	3.56	0.82	2.67	3.67	4.67	135
Male	0.98	0.12	1	1	1	333
Age	50.61	6.82	42	50	59	135
No previous employers	1.08	1.27	0	1	3	334

Table 2
The Culture of Board Members and Executive Compensation

The dependent variable is the Total compensation. All independent variables are defined in Table 1. Parameters are estimated by ordinary least squares. All regressions include 9 industry dummies but coefficients are not reported. Robust standard errors corrected for heteroskedasticity are presented in parentheses. ***, **, and * denote statistical significance at the 1, 5, and 10 percent, respectively.

	(1)	(2)	(3)	(4)	(5)	(6)
	Total compensation	Total compensation	Total compensation	Total compensation	Total compensation	Total compensation
ROA	-141129 (318754)	-101434 (305286)	-100866 (304589)	-33224 (316938)	-68042 (309511)	-9854 (374724)
Growth opportunities	-52043 (91903)	-57622 (88179)	-46740 (89205)	-36952 (87202)	-47599 (92467)	-35960 (88896)
Log market capitalization	1374416*** (162688)	1336709*** (152670)	1368229*** (160483)	1361687*** (154556)	1363287*** (159202)	1400350*** (166808)
Universalism	-375770 (350972)					-35221 (381423)
Equal treatment for everyone		273424 (222622)				
Benevolence			-430581 (404955)			-281563 (378163)
Achievement				-542273* (280399)		-1001933* (521060)
Conformity					-206594 (262695)	-711443* (427314)
Tradition						667184 (478916)
Hedonism						318279 (282329)
Stimulation						65725 (436692)
Self-direction						-470781 (514040)
Power						1225808 (802375)
Risk						-71071 (305444)
Observations	253	253	253	253	253	253
R-squared	0.42	0.42	0.42	0.42	0.42	0.45

Table 3
The Role of Ownership Structure and the Labor Market on Executive Compensation

The dependent variable is the Total compensation. All independent variables are defined in Table 1. Parameters are estimated by ordinary least squares. All regressions include 9 industry dummies but coefficients are not reported. Robust standard errors corrected for heteroskedasticity are presented in parentheses. ***, **, and * denote statistical significance at the 1, 5, and 10 percent, respectively.

	(1) Total compensation	(2) Total compensation	(3) Total compensation	(4) Total compensation	(5) Total compensation	(6) Total compensation	(7) Total compensation
ROA	-74829 (307661)	-114053 (305885)	-8574 (305382)	-58110 (491503)	1148 (289536)	-36233 (288359)	-80828 (287467)
Growth opportunities	-22647 (88657)	-25412 (89912)	-14286 (93179)	-4662 (84698)	-15316 (93845)	-27754 (77202)	-48274 (83117)
Log market capitalization	1273708*** (141733)	1269000*** (140709)	1229000*** (143807)	1139000*** (115087)	1141000*** (121127)	946174*** (112419)	997717*** (129907)
Achievement	-544757* (279712)	-536215* (278987)	-497178* (278026)	-345471 (323779)	-355620 (236537)	-409948* (226734)	-419398* (226727)
Cash flow right max	-26633** (10573)	-26581** (10501)	-25804** (10620)	-23095* (12955)	-22126** (10064)	-15180 (9599)	-14073 (9480)
Wedgemax	65668* (37097)	65208* (37028)	69552* (37779)	67839*** (22527)	67283* (37572)	48450 (34827)	49066 (35102)
No decision power		238072 (359939)					
Founder or family			-971745** (436884)	-971365** (451583)	-1020000** (453424)	-938142** (416411)	-914066** (410170)
Shareholder orientation-value				13330000*** (3195000)	13710000*** (932956)	12590000*** (999137)	12500000*** (1025000)
Friendly boards					-546382 (395698)		
US sales						133081*** (38607)	136539*** (39288)
Other foreign sales							-39381 (44511)
Observations	253	253	253	253	253	253	253
R-squared	0.44	0.44	0.45	0.49	0.49	0.52	0.53

Table 4
Robustness

The dependent variable is the Total compensation, except in column 5, where the dependent variable is short-term compensation.. All independent variables are defined in Table 1, with the exception of the following. The CEO dummy is a dummy that takes value equal to one if the executive is a CEO and takes value equal to zero if the executive is a Vice-CEO. No of responding board members is the number of board members that answered the survey for the firm in which the executive is employed. Parameters are estimated by ordinary least squares. All regressions include 9 industry dummies but coefficients are not reported. Robust standard errors corrected for heteroskedasticity are presented in parentheses. ***, **, and * denote statistical significance at the 1, 5, and 10 percent, respectively.

	(1) Total compensation	(2) Total compensation	(3) Total compensation	(4) Total compensation	(5) Short-term compensation	(6) Total compensation
ROA	-110,097 (479,357)	-82,430 (479,983)	-140,507 (447,092)	-64,537 (287,603)	-142,546 (239,024)	-329,971 (259,434)
Growth opportunities	-43,616 (85,539)	-46,381 (85,909)	-160,401 (142,449)	-56,701 (85,104)	-50,043 (73,889)	-53,727 (80,820)
Log market capitalization	1,004,318*** (134,654)	993,644*** (135,590)	989,950*** (113,687)	1,009,997*** (133,849)	991,751*** (129,764)	1,035,027*** (145,369)
Achievement	-442,368 (314,770)	-418,486 (314,985)	-85,714 (328,832)	-425,662* (232,698)	-309,636 (213,914)	-381,188* (229,784)
Cash flow right max	-14,185 (12,758)	-13,282 (13,069)	-35,905** (13,807)	-15,510 (9,805)	-16,070** (7,421)	-15,182 (9,303)
Wedgemax	50,656** (22,386)	48,709** (22,435)	44,971* (25,351)	48,951 (35,061)	40,940* (21,272)	49,677 (34,783)
Founder or family	-883,073** (439,072)	-895,947** (443,660)	-645,381 (587,051)	-936,797** (420,755)	-761,468** (295,837)	-776,519** (365,692)
Shareholder orientation-value	12,344,337*** (3,104,196)	12,523,314*** (3,110,519)	11,723,358*** (2,057,606)	12,226,958*** (1,208,806)	11,669,552*** (846,821)	12,274,093*** (1,166,550)
US sales	135,484*** (33,028)	135,869*** (33,180)	128,285*** (35,478)	135,071*** (39,217)	108,543*** (32,919)	136,552*** (38,565)
Other foreign sales	-37,947 (44,634)	-38,464 (44,842)	5,082 (37,039)	-35,340 (44,371)	-35,622 (42,434)	-53,078 (45,031)
CEO dummy	714,227 (621,109)					
CEO ownership		-522,983 (1,768,698)				
CEO achievement			-242,073 (283,270)			

CEO power			839,669***			
			(317,712)			
Male			-2,025,419*			
			(1,087,661)			
Age			3,484			
			(30,249)			
No previous employers			171,392			
			(184,206)			
No of responding board members				-83,393		
				(134,073)		
Volatility						-298,650
						(730,354)
Observations	253	253	103	253	253	250
R-squared	0.528	0.526	0.815	0.526	0.587	0.516

Table 5
The Proportion of Variable Compensation

The dependent variable is the Proportion of variable compensation. All independent variables are defined in Table 1. Parameters are estimated by ordinary least squares. All regressions include 9 industry dummies but coefficients are not reported. Robust standard errors corrected for heteroskedasticity are presented in parentheses. ***, **, and * denote statistical significance at the 1, 5, and 10 percent, respectively.

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
ROA	-0.012 (0.029)	-0.013 (0.027)	-0.015 (0.028)	-0.015 (0.028)	-0.012 (0.029)	-0.012 (0.034)	-0.014 (0.030)	-0.013 (0.029)	-0.009 (0.029)	-0.013 (0.029)	0.0176 (0.0447)
Growth opportunities	0.008 (0.009)	0.008 (0.009)	0.008 (0.009)	0.008 (0.009)	0.007 (0.009)	0.007 (0.006)	0.007 (0.009)	0.005 (0.009)	0.007 (0.009)	0.006 (0.008)	0.0186* (0.0110)
Log market capitalization	0.035*** (0.006)	0.035*** (0.006)	0.036*** (0.006)	0.036*** (0.006)	0.037*** (0.006)	0.037*** (0.008)	0.038*** (0.006)	0.028*** (0.009)	0.025*** (0.010)	0.025*** (0.009)	0.0113 (0.00890)
Achievement	-0.019 (0.026)	-0.016 (0.020)	-0.016 (0.020)	-0.016 (0.020)	-0.016 (0.020)	-0.016 (0.022)	-0.017 (0.020)	-0.019 (0.019)	-0.024 (0.019)	-0.018 (0.019)	0.0116 (0.0356)
Universalism	0.003 (0.034)										
Benevolence	-0.049 (0.033)										
Conformity	0.030 (0.028)										
Tradition	-0.021 (0.037)										
Hedonism	0.002 (0.022)										
Stimulation	-0.019 (0.025)										
Self-direction	0.022 (0.036)										
Power	0.008 (0.030)										-0.0286 (0.0362)
Risk	-0.008 (0.016)										-0.0489*** (0.0179)
Cash flow right max			-0.000 (0.001)	-0.000 (0.001)	-0.000 (0.001)	-0.000 (0.001)	-0.000 (0.001)	0.000 (0.001)	0.000 (0.001)	0.001 (0.001)	0.000980 (0.00124)
Wedgemax			-0.000 (0.002)	-0.000 (0.002)	-0.001 (0.002)	-0.001 (0.002)	-0.001 (0.002)	-0.002 (0.002)	-0.002 (0.002)	-0.002 (0.002)	-0.00567** (0.00233)
No decision power					-0.097*** (0.037)	-0.098*** (0.036)	-0.094** (0.037)	-0.091** (0.037)	-0.090** (0.038)	-0.093** (0.037)	-0.0517 (0.0529)

Board monitoring						0.009 (0.039)					
Founder of family							0.027 (0.032)				
Shareholder orientation-value							-0.016 (0.046)				
US sales								0.007*** (0.002)	0.008*** (0.003)	0.007*** (0.002)	0.00892** (0.00358)
Other foreign sales								-0.001 (0.004)	-0.002 (0.004)	-0.001 (0.004)	0.00315 (0.00329)
Volatility									-0.056 (0.048)		
CEO ownership										-0.267*** (0.065)	
CEO risk											-0.0317** (0.0127)
CEO power											0.0349 (0.0314)
Observations	253	253	253	253	253	253	253	253	250	253	101
R-squared	0.181	0.160	0.161	0.161	0.187	0.187	0.190	0.222	0.227	0.238	0.338

Table 6
Other Features of Executive Compensation

The dependent variable in columns 1 to 3 is the level of CEO perks, in column 4 it is the Retirement plan dummy, and in column 5 it is the Options dummy. All independent variables are defined in Table 1. In columns 1 to 3, parameters are estimated by ordinary least squares. In columns 4 and 5, we estimate a probit model. All regressions include 9 industry dummies but coefficients are not reported. Robust standard errors corrected for heteroskedasticity are presented in parentheses. ***, **, and * denote statistical significance at the 1, 5, and 10 percent, respectively.

	(1) Perks	(2) Perks	(3) Perks	(4) Perks	(5) Retirement plan	(6) Options
ROA	-13076 (12155)	6175 (15309)	-3,207 (26,068)	143 (25,834)	0.001 (0.070)	-0.177*** (0.051)
Growth opportunities	-1878 (2417)	-398.8 (3318)	-1,087 (4,985)	-596 (5,110)	-0.042*** (0.015)	-0.002 (0.011)
Log market capitalization	21050** (10230)	21220** (10485)	20,497*** (4,524)	19,661*** (5,320)	0.134*** (0.024)	0.053*** (0.016)
Achievement	-16489 (21536)	-25991 (28065)			0.092 (0.064)	0.032 (0.023)
Universalism		66328*** (23188)	46,567** (21,443)	42,016** (21,286)	0.136* (0.074)	-0.014 (0.033)
Benevolence		-31324 (23468)			-0.034 (0.073)	0.042 (0.099)
Conformity		-32974* (18660)	-28,969 (20,930)	-26,952 (20,925)	0.139** (0.062)	-0.040 (0.044)
Tradition		36759* (20154)	29,264 (31,492)	39,081 (31,336)	-0.195** (0.088)	0.031 (0.070)
Hedonism		-7200 (19116)			-0.011 (0.044)	0.026 (0.053)
Stimulation		-15764 (17448)			0.039 (0.057)	0.031 (0.044)
Self-direction		16850 (19087)			-0.118 (0.075)	-0.060 (0.048)
Power		36962 (29762)			-0.014 (0.080)	-0.069*** (0.019)
Risk		-33792 (20835)	-31,996*** (11,140)	-32,120*** (11,031)	0.050 (0.032)	-0.033 (0.032)
Friendly board			22,327 (26,113)			
Cash flow right max				-804 (752)	-0.001 (0.002)	-0.004*** (0.001)
Wedgemax				3,737*** (1,273)	0.002 (0.004)	0.002 (0.001)
No decision power				-23,630 (30,344)	-0.195*** (0.068)	-0.048 (0.048)
US sales				-1,448 (1,955)	-0.015** (0.006)	0.008*** (0.002)
Other foreign sales				-73 (2,537)	0.010 (0.007)	-0.020*** (0.005)
Observations	270	269	269	269	266	257
R-squared	0.09	0.16	0.15	0.182		

Table 7
The Compensation of Non-Executive Directors

The dependent variable is the Board member fee in columns 1 to 5 and the board chairman fee in column 6. All independent variables are defined in Table 1. Parameters are estimated by ordinary least squares. All regressions include 9 industry dummies but coefficients are not reported. Robust standard errors corrected for heteroskedasticity are presented in parentheses. ***, **, and * denote statistical significance at the 1, 5, and 10 percent, respectively.

	(1) Board member fee	(2) Board member fee	(3) Board member fee	(4) Board member fee	(5) Board member fee	(6) Board member fee	(7) Board chairman fee
ROA	35223 (48331)	39733 (60758)	-74271 (58521)	39731 (51279)	46757 (54023)	33927 (51256)	-11229 (15443)
Growth opportunities	2187 (18657)	717.8 (19613)	-37045** (17497)	1582 (18767)	-1946 (19179)	-539.5 (19146)	-3388 (2708)
Log market capitalization	110991***	110441***	154516***	105359***	102511***	94465***	29505***
Achievement	(18873) -97709** (44678)	(19841) -117110** (57362)	(28301) -69213 (59881)	(18697) -116322** (48002)	(18779) -109891** (47656)	(17748) -122396** (47361)	(5485) -13074 (10656)
Universalism		4090 (36705)					
Benevolence		-17682 (38327)					
Conformity		41670 (49103)					
Tradition		-22853 (51210)					
Conformity		41670 (49103)					
Hedonism		9397 (29769)					
Stimulation		29321 (36337)	74086* (43365)	50323* (29736)	59534** (28889)	54947* (29037)	6994 (10037)
Selfdirection		34747 (51645)					
Power		-17274 (80909)					
Risk		3573 (40658)					
Cash flow right max				-2291 (1437)	-2723* (1426)	-1702 (1422)	-1039*** (320)
Wedgemax				5139** (2272)	4863** (2167)	3780 (2333)	1350 (948)
Board advice					-104756*** (39762)		
Board decision power					-31332 (50276)		
US sales						8826** (3548)	613.7 (1105)
Other foreign sales						-1636 (3878)	-67.89 (1554)
CEO achievement			-36775 (34118)				
CEO stimulation			90512**				

			(37177)				
Observations	219	219	91	219	219	219	166
R-squared	0.35	0.36	0.54	0.37	0.389	0.39	0.50

Appendix

Table 1A: Summary statistics for survey respondents and nonrespondents

This table contains summary statistics of characteristics of all resident directors (1,372 individuals) of all publicly-traded firms in Sweden (286 firms) in 2005. The top panel contains summary statistics for all survey respondents. The bottom panel contains statistics for all nonrespondents. Number of directorships is the number of directorships a director holds in all publicly-traded firms including the firm the director was surveyed for. Alternate is a dummy variable which is defined to be one if the director is an alternate director. Same Industry is a dummy variable which is defined to be one if the director's primary employer in 2004 is from the same two-digit industry as the firm on whose board the director sits. Two-digit industry codes are from Statistics Sweden. All other data is from Market Manager. The differences in director characteristics between respondents and nonrespondents are significant at the 1 percent level for Number Directorships, and Age and at the 10 percent level for Alternate.

Variable	Obs	Mean	Std. Dev.	Min	Max
Survey respondents					
Number of Directorships	502	1.361	0.838	1	7
Age	502	54.203	9.405	24	73
Tenure	502	2.677	2.264	0	9
Alternate	502	0.136	0.343	0	1
Same Industry	466	0.391	0.488	0	1
Survey nonrespondents					
Number of Directorships	870	1.243	0.687	1	6
Age	870	52.024	9.787	24	80
Tenure	870	2.823	2.331	0	9
Alternate	870	0.174	0.379	0	1
Same Industry	825	0.432	0.496	0	1

Table 2A: Cultural values

Self-Direction: Independent thought and action; choosing, creating, exploring.

Stimulation: Excitement, novelty, and challenge in life.

Hedonism: Pleasure and sensuous gratification for oneself.

Achievement: Personal success through demonstrating competence according to social standards

Power: Social status and prestige, control or dominance over people and resources.

Security: Safety, harmony, and stability of society, or relationships, and of self.

Conformity: Restraint of actions, inclinations, and impulses likely to upset or harm others and violate social expectations or norms.

Tradition: Respect, commitment, and acceptance of the customs and ideas that traditional culture or religion provide the self.

Benevolence: Preserving and enhancing the welfare of those with whom one is in frequent personal contact (the "in-group").

Universalism: Understanding, appreciation, tolerance, and protection for the welfare of all people and for nature.

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Table 3A: Scenarios and Shareholder Orientation

Corporation F is a manufacturer of consumer goods. Despite considerable competition, Corporation F is a highly profitable company thanks to patented technology and manufacturing know-how. In recent years, the company has been paying out only small amounts as regular dividends. The company now contemplates ways for using its very high capital surplus.

Suppose you are a director in F. To what extent would you agree with the following propositions?

The company should...

	Strongly agree	Agree	Slightly agree	Slightly Disagree	Disagree	Strongly Disagree
reduce the price of its products to benefit consumers.						
distribute virtually all of its undistributed profits to its shareholders.						

Corporation D has a loss-making business in the mass media market. Although it has a well-known brand name, D's production technology is now obsolete and its workers are relatively old. The only way to avoid further losses is to cease operations and wind up the company, in which case a substantial amount of proceeds will remain after creditors were paid and workers received their legal severance payments.

Suppose you are a director in D. To what extent would you agree with the following propositions?

After ceasing operations and satisfying legal financial obligations, the company should...

	Strongly agree	Agree	Slightly agree	Slightly Disagree	Disagree	Strongly Disagree
distribute all the remaining proceeds as dividend to its shareholders.						
devote half of the balance to its workers, in proportion to their service in D, to alleviate their hardship.						

Corporation M conducts business in the entertainment industry through several wholly-owned profitable subsidiaries. The company manages to service its debt but its financial situation is tight. Corporation M learns that the vast majority of its shareholders, holding over 98% of its shares, are in need for cash.

Suppose you are a director in M. To what extent would you agree with the following propositions?

The company should...

	Strongly agree	Agree	Slightly agree	Slightly Disagree	Disagree	Strongly Disagree
sell one of its subsidiaries for a "firesale" (very low) price to finance a dividend distribution to its shareholders notwithstanding the risk of financial default.						
avoid any kind of distribution to shareholders as long as the company is in the vicinity of insolvency.						

Corporation C operates a large recreation center in an urban area, which is open until 7 pm. Even though longer opening hours are now industry standard and would be profitable, the company has

opted against it in order to preserve the character of surrounding neighborhoods. One of C's shareholders calls for changing this policy to increase profits.

Suppose you are a director in C. To what extent would you agree with the following propositions?
The company should...

	Strongly agree	Agree	Slightly agree	Slightly Disagree	Disagree	Strongly Disagree
open its center for as many days and hours as is financially profitable.						
adhere to its current policy on hours of operation.						

Corporation X is considering updating its website. A consultant proposes to post one of the following statements under "Corporate Philosophy" as a statement from the board of directors.

Suppose you are a director in X. To what extent would you agree with the following propositions?

The company should adopt the following statement as its corporate philosophy and post it on its website.

	Strongly agree	Agree	Slightly agree	Slightly Disagree	Disagree	Strongly Disagree
"We believe that our corporation should have one overriding purpose – to create value for shareholders. If every corporation were faithful to this mission, as we are, the net long-term result would be a vibrant economy that produces the greatest prosperity for the greatest number."						
"We believe that our corporation should strive to achieve a variety of sometimes conflicting goals. These include providing competitive returns to shareholders, ensuring fair treatment of employees, behaving responsibly towards customers, maintaining good relationships with suppliers and local communities, and pursuing reliable social and environmental policies. If every corporation were faithful to these multiple missions, as we are, the net long-term result would be a fundamentally more decent and just society."						