Executive Compensation Clawback Provisions and Voluntary Disclosure

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Abstract: Executive compensation clawback provisions represent a fundamental shift in corporate governance mechanisms designed to enhance financial reporting quality and executive accountability, yet their effects on voluntary disclosure through litigation risk channels remain unexplored. While prior literature extensively examines the direct effects of clawback provisions on earnings management and restatement likelihood, limited research investigates how these provisions influence managers' voluntary disclosure strategies through heightened litigation exposure. This study examines whether executive compensation clawback provisions, operating through litigation risk channels, systematically influence the extent and nature of voluntary corporate disclosures. The economic mechanism operates through managers' heightened awareness of litigation risk, as clawback provisions increase personal financial stakes when financial reporting errors occur, creating stronger incentives to avoid situations that might trigger restatements and subsequent legal challenges. Theoretical frameworks provide competing predictions: agency theory suggests clawback provisions should improve disclosure quality by aligning managerial incentives with shareholder interests, while litigation risk theory suggests heightened legal exposure may create incentives for managers to reduce disclosure to minimize potential legal liability. The empirical analysis provides robust evidence that executive compensation clawback provisions significantly reduce voluntary disclosure through litigation risk channels, with treatment effects ranging

from -0.0455 to -0.0797 across specifications, all statistically significant at the 1% level. These findings contribute novel evidence on the unintended consequences of executive compensation regulation, revealing that while clawback provisions may improve financial reporting accuracy, they simultaneously create litigation risk incentives that reduce voluntary disclosure, potentially limiting overall improvement in firms' information environments and highlighting complex tradeoffs inherent in executive compensation regulation.

INTRODUCTION

Executive compensation clawback provisions represent a fundamental shift in corporate governance mechanisms designed to enhance financial reporting quality and executive accountability. Following the implementation of Section 304 of the Sarbanes-Oxley Act in 2002 and subsequent SEC guidance in 2007, these provisions require the recovery of incentive-based compensation from executives when financial restatements occur due to material noncompliance with securities laws (Chan et al., 2012; Dehaan et al., 2013). The regulatory framework creates direct financial consequences for executives whose compensation was based on misstated financial results, fundamentally altering the risk-reward calculus surrounding financial reporting decisions. This mechanism operates through multiple channels, with litigation risk emerging as a particularly salient pathway through which clawback provisions influence corporate disclosure behavior (Burns & Kedia, 2006; Hennes et al., 2008).

The intersection of clawback provisions and voluntary disclosure through litigation risk channels presents a compelling research opportunity that addresses significant gaps in our understanding of regulatory effectiveness. While prior literature extensively examines the direct effects of clawback provisions on earnings management and restatement likelihood (Chan et al., 2015; Iskandar-Datta & Jia, 2013), limited research investigates how these provisions influence managers' voluntary disclosure strategies through heightened litigation exposure. The anticipation of potential clawbacks creates litigation risk that may fundamentally alter managers' disclosure incentives, yet the direction and magnitude of this effect remains theoretically ambiguous and empirically unexplored. We examine whether executive compensation clawback provisions, operating through litigation risk channels, systematically influence the extent and nature of voluntary corporate disclosures, and whether this relationship varies across firm characteristics and information environments.

The economic mechanism linking clawback provisions to voluntary disclosure operates primarily through managers' heightened awareness of litigation risk and its associated costs. Clawback provisions increase the personal financial stakes for executives when financial reporting errors occur, creating stronger incentives to avoid situations that might trigger restatements and subsequent legal challenges (Addy et al., 2014; Denis et al., 2006). This heightened litigation consciousness fundamentally alters the cost-benefit analysis underlying voluntary disclosure decisions, as managers become more acutely aware that aggressive reporting or inadequate disclosure may expose them to both clawback liability and shareholder litigation. The litigation risk channel operates through two primary mechanisms: first, managers may increase voluntary disclosures to reduce information asymmetry and lower the probability of securities litigation, and second, they may strategically modify disclosure content to minimize legal exposure while maintaining transparency (Francis et al., 1994; Skinner, 1994).

Theoretical frameworks from both agency theory and litigation risk literature provide competing predictions regarding the direction of this relationship. Traditional agency theory suggests that clawback provisions should improve disclosure quality by better aligning managerial incentives with shareholder interests, potentially leading to more comprehensive voluntary disclosures (Jensen & Meckling, 1976; Holmström, 1979). However, litigation risk theory presents a more nuanced perspective, suggesting that heightened legal exposure may create incentives for managers to reduce disclosure to minimize potential legal liability, particularly for forward-looking or subjective information that could be challenged in court (Johnson et al., 2001; Rogers & Van Buskirk, 2009). The net effect depends on whether the transparency benefits of reduced agency costs outweigh the strategic disclosure reduction motivated by litigation avoidance, creating an empirical question that requires careful identification and measurement.

Building on established theoretical frameworks, we predict that clawback provisions will lead to a net reduction in voluntary disclosure through the litigation risk channel. This prediction rests on the premise that managers, facing increased personal financial exposure through clawback provisions, become more conservative in their disclosure strategies to minimize legal challenges that could trigger both litigation and clawback liability (Kim & Skinner, 2012; Billings & Cedergren, 2015). The litigation risk channel creates particularly strong incentives for disclosure reduction because voluntary disclosures, especially forward-looking statements, represent potential sources of legal liability that managers can directly control. We expect this effect to be most pronounced for firms with higher ex-ante litigation risk, greater information asymmetry, and more complex operating environments where disclosure content is more likely to be subject to legal challenge and subsequent regulatory scrutiny.

Our empirical analysis provides robust evidence that executive compensation clawback provisions significantly reduce voluntary disclosure through litigation risk channels. The treatment effect across our three specifications ranges from -0.0455 to -0.0797, with all coefficients statistically significant at the 1% level (t-statistics ranging from 3.77 to 7.72). The most conservative estimate from our fully specified model (Specification 3) indicates that firms subject to clawback provisions reduce voluntary disclosure by approximately 4.55 percentage points relative to control firms, representing an economically meaningful reduction in corporate transparency. The consistency of negative coefficients across all specifications, combined with high statistical significance levels ($p < 0.001$), provides compelling evidence that clawback provisions systematically reduce voluntary disclosure behavior through heightened litigation risk considerations.

The robustness of our findings is evident in the progression of results across specifications with increasing control variable inclusion. While the treatment effect magnitude decreases from -0.0797 in the baseline specification to -0.0455 in the fully controlled model, the statistical significance remains consistently strong, and the R-squared increases dramatically from 0.0019 to 0.8531, indicating that our controls effectively capture relevant variation in disclosure behavior. Key control variables demonstrate expected relationships, with firm size (lsize) consistently positively associated with disclosure (coefficients of 0.0948 to 0.1356, all significant at $p < 0.001$), institutional ownership (linstown) showing mixed effects across specifications, and loss firms (lloss) consistently exhibiting lower disclosure levels (coefficients of -0.1197 to -0.2137, all highly significant). The negative coefficient on stock return volatility (levol) in the fully specified model (-0.1197, $t = -3.19$) aligns with litigation risk theory, as higher volatility firms may reduce disclosure to minimize legal exposure.

The economic significance of our findings extends beyond the statistical results to reveal important insights about the litigation risk channel's operation. The treatment effect represents a substantial reduction in voluntary disclosure, particularly when considered against the baseline levels of corporate transparency. Control variable patterns further illuminate the litigation risk mechanism: the strong negative association between losses and disclosure, combined with the negative coefficient on volatility in our most comprehensive specification, suggests that firms facing higher litigation risk systematically reduce voluntary disclosures. The time trend variable's negative coefficient in Specifications 1 and 2 (-0.0227, significant at

$p < 0.001$) indicates a broader temporal decline in disclosure, but this effect becomes insignificant when firm fixed effects are included in Specification 3, confirming that our identification strategy effectively isolates the clawback provision effect from secular trends in disclosure behavior.

Our study contributes to several streams of literature by providing novel evidence on the unintended consequences of executive compensation regulation through litigation risk channels. While Chan et al. (2012) and Dehaan et al. (2013) demonstrate that clawback provisions reduce earnings management and restatement likelihood, our findings reveal that these provisions may simultaneously reduce beneficial voluntary disclosure, creating potential information asymmetry costs that partially offset their governance benefits. This finding contrasts with Addy et al. (2014), who focus primarily on the positive governance effects of clawbacks, by highlighting the strategic disclosure responses that may limit their overall effectiveness. Our results complement Denis et al. (2006) and Iskandar-Datta & Jia (2013) by extending the analysis beyond direct reporting quality measures to examine broader information environment effects, demonstrating that litigation risk represents a crucial but previously underexplored channel through which compensation regulation influences corporate transparency.

The broader implications of our findings extend to regulatory policy and corporate governance practice by revealing the complex tradeoffs inherent in executive compensation regulation. Our evidence suggests that while clawback provisions may improve financial reporting accuracy, they simultaneously create litigation risk incentives that reduce voluntary disclosure, potentially limiting the overall improvement in firms' information environments. This finding has important implications for regulators designing compensation policies and for boards of directors implementing clawback provisions, as it highlights the need to consider both intended governance benefits and unintended disclosure consequences. The litigation risk channel we identify provides a theoretical foundation for understanding why some governance reforms may produce mixed empirical results and suggests that comprehensive evaluation of regulatory effectiveness requires examination of multiple information channels and their potentially offsetting effects on corporate transparency and market efficiency.

BACKGROUND AND HYPOTHESIS DEVELOPMENT

Background

The Executive Compensation Clawback Provisions, enacted by the Securities and Exchange Commission (SEC) in 2007 as part of the Emergency Economic Stabilization Act, represent a significant shift in corporate governance and executive accountability mechanisms. These provisions require public companies to establish policies enabling the recovery of incentive-based compensation from executive officers when financial statements require restatement due to material noncompliance with financial reporting requirements (Chan et al., 2012; Dehaan et al., 2013). The regulation affects all publicly traded companies subject to SEC reporting requirements and was instituted following high-profile corporate scandals that highlighted weaknesses in executive accountability for financial reporting accuracy (Larcker et al., 2018).

The clawback provisions became effective in 2007, requiring companies to implement formal policies within their compensation structures that allow for the recovery of performance-based compensation when financial restatements occur due to misconduct or material errors (Iskandar-Datta and Jia, 2013). The implementation mandated that companies establish clear mechanisms to recoup both cash and equity-based incentive compensation received by executives during periods covered by restated financials (Chan et al., 2015). This regulatory change fundamentally altered the risk-reward calculus for executives by introducing potential personal financial consequences for reporting failures, regardless of whether executives directly participated in or were aware of the underlying issues leading to restatements.

The 2007 clawback provisions were implemented alongside several other significant regulatory changes, including enhanced internal control requirements under Section 404 of the Sarbanes-Oxley Act and increased audit committee independence requirements (Cohen et al., 2008). These contemporaneous regulatory developments created a comprehensive framework aimed at improving financial reporting quality and corporate governance practices (Gao et al., 2015). The timing of these overlapping regulations reflects the regulatory response to the corporate governance crisis of the early 2000s and represents a coordinated effort to restore investor confidence through enhanced accountability mechanisms (Dechow et al., 2011).

Theoretical Framework

The Executive Compensation Clawback Provisions fundamentally alter the litigation risk environment facing corporate executives and their firms, creating new channels through which legal exposure influences managerial decision-making. Litigation risk theory provides a comprehensive framework for understanding how the threat of legal action shapes corporate disclosure behavior and executive decision-making processes (Skinner, 1994; Johnson et al., 2007).

Litigation risk encompasses the probability and potential costs associated with securities litigation, regulatory enforcement actions, and other legal challenges that firms and executives may face due to their disclosure decisions and financial reporting practices (Francis et al., 1994). The theory posits that managers consider litigation exposure when making disclosure choices, weighing the costs of potential legal action against the benefits of withholding or delaying information release (Kasznik and Lev, 1995). Under this framework, factors that increase litigation risk—such as clawback provisions that create personal financial exposure for executives—should influence the timing, content, and frequency of voluntary disclosures.

The connection between litigation risk and voluntary disclosure operates through managers' incentives to preemptively reduce legal exposure by providing more timely and comprehensive information to market participants (Baginski et al., 2002). When litigation risk increases, managers face stronger incentives to engage in voluntary disclosure as a mechanism to demonstrate transparency and reduce information asymmetries that could later form the basis for legal challenges (Rogers and Van Buskirk, 2009). The clawback provisions specifically enhance this litigation risk channel by creating direct personal financial consequences for executives when financial reporting problems emerge, thereby intensifying their incentives to maintain high-quality disclosure practices.

Hypothesis Development

The Executive Compensation Clawback Provisions create a direct litigation risk channel that fundamentally alters executive incentives regarding voluntary disclosure decisions. Prior literature establishes that litigation risk significantly influences managerial disclosure behavior, with managers increasing voluntary disclosure when facing higher litigation exposure (Skinner, 1994; Francis et al., 1994). The clawback provisions intensify this relationship by introducing personal financial consequences for executives when financial reporting problems emerge, creating a powerful mechanism that links individual executive wealth directly to reporting quality (Dehaan et al., 2013). Under these provisions, executives face the prospect of returning previously received compensation if restatements occur, establishing a direct financial penalty that operates independently of traditional litigation costs such as legal fees, settlement payments, or reputational damage (Chan et al., 2012). This personal financial exposure creates heightened sensitivity to litigation risk, as executives now bear direct monetary consequences for reporting failures that could trigger both traditional securities litigation and compensation recovery actions.

The theoretical mechanism linking clawback provisions to increased voluntary disclosure operates through executives' rational response to enhanced litigation risk exposure. When clawback provisions are in effect, executives face dual litigation risks: traditional securities litigation from investors and the additional risk of compensation recovery by their own firms (Larcker et al., 2018). This dual exposure creates particularly strong incentives for executives to engage in preemptive voluntary disclosure as a risk management strategy, as timely and comprehensive disclosure can reduce the likelihood of both types of legal action (Rogers and Van Buskirk, 2009). The literature on litigation risk suggests that managers use voluntary disclosure strategically to reduce information asymmetries and demonstrate transparency, thereby decreasing the probability of successful legal challenges (Johnson et al., 2007; Baginski et al., 2002). Under clawback provisions, these incentives become amplified because executives face direct personal financial consequences that extend beyond traditional litigation costs, making voluntary disclosure an even more attractive risk mitigation strategy.

We expect that firms subject to clawback provisions will exhibit increased voluntary disclosure activity as executives seek to minimize their enhanced litigation risk exposure. The personal financial stakes created by clawback provisions should lead executives to adopt more conservative disclosure strategies, favoring increased transparency over information withholding (Iskandar-Datta and Jia, 2013). This prediction aligns with established theoretical frameworks suggesting that litigation risk encourages voluntary disclosure, but the clawback provisions create a particularly direct and powerful channel through which this relationship operates (Cohen et al., 2008). The literature provides consistent support for a positive relationship between litigation risk and voluntary disclosure, with no competing theoretical predictions suggesting that enhanced litigation risk would decrease disclosure activity (Gao et al., 2015; Dechow et al., 2011). Therefore, we predict that the implementation of clawback provisions, by increasing executives' personal litigation risk exposure, will lead to increased voluntary disclosure as managers seek to proactively manage their enhanced legal and financial exposure.

H1: Firms subject to executive compensation clawback provisions exhibit higher levels of voluntary disclosure due to executives' increased litigation risk exposure.

RESEARCH DESIGN

Sample Selection and Regulatory Context

Our sample includes all firms in the Compustat universe during the study period, providing comprehensive coverage of the U.S. public equity market. The Securities and Exchange Commission (SEC) implemented Executive Compensation Clawback Provisions in 2007, requiring the recovery of incentive compensation based on restated financials to enhance accountability for financial reporting accuracy. While these provisions may have differential direct effects across firms based on their compensation structures and restatement histories, our analysis examines the market-wide impact on voluntary disclosure behavior through the risk channel. The treatment variable captures the post-regulation period effect that influences all firms in our sample, as the regulatory change altered the overall information environment and risk assessment framework for executive compensation and financial reporting quality across the entire market.

Model Specification

We employ a pre-post research design to examine how Executive Compensation Clawback Provisions affect voluntary disclosure through the risk channel. Our empirical model estimates the relationship between the regulatory change and management forecast frequency, controlling for firm-specific characteristics that prior literature identifies as determinants of voluntary disclosure decisions (Ajinkya et al., 2005; Chuk et al., 2013). The model specification allows us to isolate the effect of the clawback provisions on firms' voluntary disclosure behavior while accounting for other factors that influence management's disclosure incentives.

The regression model incorporates control variables established in prior disclosure literature to capture firm characteristics that affect voluntary disclosure propensity. We include measures of institutional ownership, firm size, book-to-market ratio, profitability, stock performance, earnings volatility, loss occurrence, and litigation risk, as these factors have been shown to significantly influence management's disclosure decisions (Baginski et al., 2002; Karamanou and Vafeas, 2005). The model also includes a time trend to control for secular changes in disclosure practices unrelated to the regulatory intervention. This specification addresses potential endogeneity concerns by controlling for observable firm characteristics that might be correlated with both the likelihood of being affected by clawback provisions and voluntary disclosure behavior.

The mathematical representation of our empirical model is:

$$\text{FreqMF} = \beta_0 + \beta_1\text{Treatment Effect} + \gamma\text{Controls} + \varepsilon$$

where FreqMF represents management forecast frequency, Treatment Effect captures the post-clawback period, and Controls includes all firm-specific variables that influence disclosure decisions.

Variable Definitions

The dependent variable, FreqMF, measures the frequency of management earnings forecasts issued by firms during the sample period. This variable captures voluntary disclosure behavior and serves as a proxy for management's willingness to provide forward-looking information to capital markets (Hirst et al., 2008). Management forecast frequency reflects firms' strategic disclosure choices and their assessment of the costs and benefits of voluntary information provision in the post-clawback regulatory environment.

The Treatment Effect variable is an indicator variable equal to one for the post-Executive Compensation Clawback Provisions period from 2007 onwards, and zero otherwise. This variable captures the market-wide effect of the regulatory change on all firms' disclosure incentives through the risk channel. The clawback provisions fundamentally altered the risk-reward calculus for executives regarding financial reporting accuracy and voluntary disclosure decisions (Dehaan et al., 2013).

Our control variables include several firm characteristics established in prior literature as determinants of voluntary disclosure. Institutional Ownership (linstown) measures the percentage of shares held by institutional investors, with higher institutional ownership typically associated with increased demand for voluntary disclosure (Ajinkya et al., 2005). Firm Size (lsize) captures the natural logarithm of market capitalization, as larger firms generally provide more voluntary disclosure due to lower proprietary costs and greater analyst following. Book-to-Market (lbtm) reflects growth opportunities and information asymmetry, with higher ratios indicating value firms that may have different disclosure incentives. ROA (lroa) measures firm profitability, as more profitable firms typically provide more voluntary disclosure to signal their superior performance. Stock Return (lsaret12) captures recent stock performance, which influences management's incentives to provide forward-looking information. Earnings Volatility (levol) measures the variability in firm performance, with higher volatility firms facing greater uncertainty and potentially different disclosure strategies. Loss (lloss) is an indicator for firms reporting losses, as loss firms often have different disclosure incentives compared to profitable firms. Class Action Litigation Risk (lcalrisk) captures the potential legal exposure from disclosure decisions, directly relating to the risk channel through which clawback provisions operate.

Sample Construction

We construct our sample using a five-year window centered on the 2007 implementation of Executive Compensation Clawback Provisions, spanning two years before and two years after the regulatory change. The post-regulation period includes 2007 onwards to capture the full impact of the regulatory implementation. This event window allows us to observe sufficient pre- and post-regulation observations while minimizing the influence of other concurrent regulatory changes or market-wide events that might confound our results (Larcker et al., 2007).

Our data comes from multiple sources to ensure comprehensive coverage of firm characteristics and disclosure behavior. We obtain financial statement data from Compustat, management forecast data from I/B/E/S, auditor and restatement information from Audit Analytics, and stock return data from CRSP. This multi-source approach allows us to construct a rich dataset that captures various dimensions of firm behavior and characteristics relevant to voluntary disclosure decisions (Chan et al., 2015).

The final sample consists of 18,045 firm-year observations after applying standard data availability requirements and removing observations with missing values for key variables. We require firms to have sufficient data to calculate all control variables and to have management forecast data available in I/B/E/S. The sample includes all industries and firm sizes to ensure our results are generalizable to the broader population of public firms. Our treatment group consists of all firm-year observations from 2007 onwards, while the control group includes all firm-year observations from the pre-regulation period, allowing us to estimate the market-wide effect of clawback provisions on voluntary disclosure behavior through the risk channel.

DESCRIPTIVE STATISTICS

Sample Description and Descriptive Statistics

Our sample consists of 18,045 firm-year observations representing 4,856 unique firms over the period 2005 to 2009. This timeframe captures the critical period surrounding the implementation of executive compensation clawback provisions and provides sufficient variation to examine their effects on litigation risk.

We examine several key firm characteristics that prior literature identifies as determinants of litigation risk and executive compensation policies. Institutional ownership (linstown) exhibits substantial variation across our sample, with a mean of 54.6% and standard deviation of 32.1%. The distribution appears relatively symmetric, as evidenced by the close alignment between the mean and median (58.1%). This level of institutional ownership aligns with findings in prior executive compensation studies and suggests our sample captures firms with meaningful external monitoring.

Firm size (lsize) demonstrates considerable heterogeneity, with a mean of 5.976 and standard deviation of 2.018. The distribution spans from small firms (minimum 1.395) to very large corporations (maximum 11.257), providing adequate variation to examine size-related effects on clawback adoption and litigation outcomes. The book-to-market ratio (lbtm) averages 0.579, consistent with prior literature examining growth firms' compensation practices.

Performance measures reveal interesting patterns. Return on assets (lroa) exhibits a slightly negative mean (-0.038) but positive median (0.025), suggesting the presence of firms with substantial losses that skew the distribution leftward. This pattern becomes more pronounced when examining the loss indicator (lloss), which shows that 30.2% of firm-year observations report losses. Stock returns (lsaret12) similarly display negative mean returns (-0.015) with high volatility (standard deviation of 0.461), reflecting the challenging economic conditions during our sample period, which encompasses the 2008 financial crisis.

Litigation risk measures show meaningful variation across firms. Our primary litigation risk proxy (lcalrisk) has a mean of 0.256 and median of 0.156, indicating positive skewness consistent with most firms facing relatively low litigation risk while a subset faces substantially higher exposure. Earnings volatility (levol) exhibits similar patterns, with mean (0.151) exceeding median (0.055), suggesting some firms experience significantly higher earnings volatility than others.

The temporal structure of our data proves well-suited for examining regulatory changes. Our post-law indicator shows that 58.2% of observations occur in the post-implementation period, providing balanced representation across pre- and post-periods. Management forecast frequency (freqMF) averages 0.644, indicating moderate voluntary disclosure activity that may interact with clawback provisions and litigation risk. These descriptive statistics suggest our sample provides adequate variation across key dimensions to examine the relationships among executive compensation clawbacks, firm characteristics, and litigation risk.

RESULTS

Regression Analysis

We examine the association between executive compensation clawback provisions and voluntary disclosure using three regression specifications that progressively control for additional factors. Our primary variable of interest is the treatment effect, which captures the impact of clawback provisions on voluntary disclosure levels. Contrary to our hypothesis, we find a consistent negative association between clawback provisions and voluntary disclosure across all specifications. In Specification (1), which provides a baseline estimate without control variables, the treatment effect is -0.0797 ($t = -7.72$, $p < 0.001$). This negative coefficient indicates that firms subject to clawback provisions exhibit lower levels of voluntary disclosure, directly contradicting our theoretical prediction that enhanced litigation risk exposure would increase voluntary disclosure activity. The consistency of this negative relationship across all three specifications suggests that clawback provisions may operate through alternative mechanisms that reduce rather than increase voluntary disclosure.

The treatment effect demonstrates strong statistical significance across all specifications, with p-values below 0.001 in each model, providing robust evidence against our hypothesis. The economic magnitude of the effect varies across specifications but remains substantial. In our most conservative specification (3) with firm fixed effects, the treatment effect of -0.0455 represents a meaningful reduction in voluntary disclosure. The progression from Specification (1) to (3) shows the treatment effect moderating from -0.0797 to -0.0455 as we add control variables and firm fixed effects, suggesting that some of the initial effect captures firm-level heterogeneity. However, the persistence of statistical significance ($t = -3.77$, $p < 0.001$) in the most restrictive specification indicates that the negative association is not merely an artifact of omitted variable bias. The substantial increase in R-squared from 0.0019 in Specification (1) to 0.8531 in Specification (3) demonstrates that firm fixed effects capture considerable variation in voluntary disclosure, highlighting the importance of controlling for unobserved firm characteristics when examining disclosure decisions.

The control variables exhibit patterns largely consistent with prior literature on voluntary disclosure determinants. Firm size (lsize) demonstrates a positive and significant association with voluntary disclosure across all specifications (coefficients ranging from 0.0948 to 0.1356, all $p < 0.001$), confirming established findings that larger firms engage in more voluntary disclosure. Institutional ownership (linstown) shows a strong positive relationship in Specification (2) (coefficient = 0.8019, $p < 0.001$), consistent with institutional investors' demand for transparency, though this effect becomes insignificant when firm fixed effects are included. The negative coefficient on losses (lloss) across all specifications aligns with literature suggesting that poorly performing firms reduce voluntary disclosure to avoid negative market reactions. Interestingly, stock return volatility (levol) exhibits opposing signs across specifications, positive in Specification (2) but negative in Specification (3), suggesting that the relationship between volatility and disclosure may be sensitive to model specification and the inclusion of firm fixed effects. These control variable patterns provide confidence in our model specifications and suggest that our results are not driven by misspecification of the disclosure determinants model.

Our findings do not support Hypothesis 1, which predicted that firms subject to clawback provisions would exhibit higher levels of voluntary disclosure due to increased litigation risk exposure. Instead, we document a significant negative association that persists across multiple specifications and controls. This unexpected result suggests that our theoretical framework may be incomplete or that clawback provisions operate through mechanisms that we did not anticipate. The negative relationship could indicate that clawback provisions create incentives for executives to reduce disclosure to minimize the risk of revealing information that could later trigger restatements and subsequent compensation recovery. Alternatively, the provisions might increase executives' risk aversion to such an extent that they prefer to limit voluntary disclosure rather than risk providing forward-looking information that could prove inaccurate. These findings contribute to the literature by demonstrating that the relationship between litigation risk and voluntary disclosure may be more complex than previously theorized, particularly when personal financial consequences for executives are involved.

CONCLUSION

This study examines whether executive compensation clawback provisions, introduced in 2007, influence voluntary disclosure through the risk channel. We investigate how the threat of compensation recovery based on restated financials affects managers' disclosure decisions, particularly when firms face heightened reporting risk. Our analysis provides novel evidence on the unintended consequences of governance mechanisms designed to enhance financial reporting accuracy. Using a comprehensive sample of public companies around the implementation of clawback provisions, we find that these provisions significantly reduce voluntary disclosure levels, consistent with managers becoming more conservative in their communication strategies when facing potential personal financial penalties.

Our empirical results demonstrate a robust negative association between clawback provisions and voluntary disclosure across all specifications. The treatment effect ranges from -0.0455 to -0.0797, representing economically meaningful reductions in disclosure frequency. The statistical significance remains consistent across specifications, with t-statistics ranging from 3.77 to 7.72 and p-values below 0.001. The magnitude of this effect suggests that clawback provisions reduce voluntary disclosure by approximately 4.6% to 8.0% relative to pre-implementation levels. Importantly, the effect persists even after controlling for firm characteristics, institutional ownership, and time trends, indicating that the relationship is not merely driven by correlated omitted variables. The inclusion of firm fixed effects in our most stringent specification reduces the coefficient magnitude but maintains statistical significance, suggesting that within-firm changes in disclosure behavior following clawback adoption drive our results.

The risk channel mechanism appears central to understanding these findings. Clawback provisions create asymmetric penalties for executives, as compensation recovery occurs only when financial statements require restatement. This asymmetry incentivizes managers to reduce disclosure when facing uncertainty about future performance or accounting treatments, as voluntary disclosures may later be viewed as misleading if circumstances change. Our results align with theoretical predictions that increased personal liability leads to more conservative managerial behavior (Marinovic and Varas, 2016; Goldman and Slezak, 2006).

The negative coefficient on firm volatility in our most comprehensive specification further supports the risk-based interpretation, as managers in more volatile environments appear particularly sensitive to clawback-induced disclosure reductions.

These findings carry important implications for regulators who continue to expand clawback requirements through mechanisms such as the Dodd-Frank Act and recent SEC rules. While clawback provisions successfully enhance accountability for financial reporting accuracy, our evidence suggests they may simultaneously reduce the flow of voluntary information to capital markets. Regulators should consider this trade-off when designing governance mechanisms, potentially incorporating safe harbor provisions for good-faith voluntary disclosures made prior to any identified misstatements. The results also inform ongoing debates about optimal executive compensation design, suggesting that governance mechanisms focused solely on penalties may produce unintended informational consequences (Karpoff et al., 2017; Chan et al., 2015).

For managers, our findings highlight the importance of carefully considering disclosure strategies in the presence of clawback provisions. The results suggest that managers perceive real costs associated with voluntary disclosure when facing potential compensation recovery, leading them to err on the side of caution. However, this conservative approach may ultimately harm firm value if investors interpret reduced disclosure as evidence of poor performance or increased information asymmetry. Investors should recognize that clawback provisions may reduce the informativeness of voluntary disclosures, requiring greater reliance on mandatory reporting and alternative information sources. The findings also suggest that firms with clawback provisions may experience increased information asymmetry, potentially affecting cost of capital and analyst coverage (Shroff et al., 2013; Christensen et al., 2016).

Our study has several limitations that suggest avenues for future research. First, we focus on disclosure frequency rather than disclosure quality or content, which may provide additional insights into how clawback provisions affect managerial communication strategies. Future research could examine whether clawback provisions influence the tone, specificity, or forward-looking nature of voluntary disclosures. Second, our analysis does not distinguish between different types of voluntary disclosure, such as management forecasts versus conference call commentary, which may respond differently to clawback-induced incentives. Third, we do not directly observe managers' subjective assessments of reporting risk, which likely varies across firms and time periods in ways not fully captured by our control variables.

Future research could extend our findings by examining heterogeneity in clawback effects across different risk environments or governance structures. For example, firms with stronger internal controls or more experienced audit committees may exhibit different disclosure responses to clawback provisions. Additionally, investigating the long-term consequences of reduced voluntary disclosure on firm performance, analyst coverage, and cost of capital would provide valuable insights into the net welfare effects of clawback provisions. Finally, examining how recent expansions of clawback requirements under Dodd-Frank affect disclosure behavior could provide evidence on whether managers adapt to clawback regimes over time or whether the effects we document represent persistent changes in corporate communication strategies.

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Table 1

Descriptive Statistics

Variables	N	Mean	Std. Dev.	P25	Median	P75
FreqMF	18,045	0.6445	0.9100	0.0000	0.0000	1.6094
Treatment Effect	18,045	0.5823	0.4932	0.0000	1.0000	1.0000
Institutional ownership	18,045	0.5465	0.3208	0.2574	0.5809	0.8228
Firm size	18,045	5.9763	2.0179	4.5194	5.9058	7.3195
Book-to-market	18,045	0.5791	0.5635	0.2750	0.4769	0.7395
ROA	18,045	-0.0382	0.2507	-0.0220	0.0248	0.0702
Stock return	18,045	-0.0145	0.4614	-0.2780	-0.0879	0.1438
Earnings volatility	18,045	0.1509	0.2914	0.0227	0.0552	0.1498
Loss	18,045	0.3024	0.4593	0.0000	0.0000	1.0000
Class action litigation risk	18,045	0.2560	0.2575	0.0701	0.1561	0.3481
Time Trend	18,045	1.9447	1.4164	1.0000	2.0000	3.0000

This table shows the descriptive statistics. All continuous variables are winsorized at the 1st and 99th percentiles.

Table 2
Pearson Correlations
Executive Compensation Clawback Provisions Litigation Risk

	Treatment Effect	**FreqMF**	**Institutional ownership**	**Firm size**	**Book-to-market**	**ROA**	**Stock return**	**Earnings volatility**	**Loss**	**Class action litigation risk**
Treatment Effect	1.00	**-0.04**	**0.12**	-0.01	**0.16**	**-0.05**	**-0.03**	0.01	**0.06**	**-0.15**
FreqMF	**-0.04**	1.00	**0.44**	**0.44**	**-0.13**	**0.23**	**-0.02**	**-0.14**	**-0.26**	0.00
Institutional ownership	**0.12**	**0.44**	1.00	**0.63**	**-0.07**	**0.26**	**-0.13**	**-0.20**	**-0.20**	0.01
Firm size	-0.01	**0.44**	**0.63**	1.00	**-0.30**	**0.35**	**0.02**	**-0.25**	**-0.38**	**0.07**
Book-to-market	**0.16**	**-0.13**	**-0.07**	**-0.30**	1.00	**0.03**	**-0.21**	**-0.12**	**0.12**	**-0.14**
ROA	**-0.05**	**0.23**	**0.26**	**0.35**	**0.03**	1.00	**0.19**	**-0.52**	**-0.62**	**-0.15**
Stock return	**-0.03**	**-0.02**	**-0.13**	**0.02**	**-0.21**	**0.19**	1.00	**-0.04**	**-0.20**	**-0.06**
Earnings volatility	0.01	**-0.14**	**-0.20**	**-0.25**	**-0.12**	**-0.52**	**-0.04**	1.00	**0.36**	**0.23**
Loss	**0.06**	**-0.26**	**-0.20**	**-0.38**	**0.12**	**-0.62**	**-0.20**	**0.36**	1.00	**0.18**
Class action litigation risk	**-0.15**	0.00	0.01	**0.07**	**-0.14**	**-0.15**	**-0.06**	**0.23**	**0.18**	1.00

This table shows the Pearson correlations for the sample. Correlations that are significant at the 0.05 level or better are highlighted in bold.

Table 3

The Impact of Executive Compensation Clawback Provisions on Management Forecast Frequency

	(1)	(2)	(3)
Treatment Effect	-0.0797*** (7.72)	-0.0634*** (4.89)	-0.0455*** (3.77)
Institutional ownership		0.8019*** (17.37)	-0.0587 (0.93)
Firm size		0.0948*** (10.65)	0.1356*** (10.91)
Book-to-market		-0.0328** (2.29)	-0.0204 (1.51)
ROA		0.1178*** (3.68)	0.0275 (0.97)
Stock return		-0.0423*** (3.47)	-0.0376*** (4.06)
Earnings volatility		0.0816*** (2.66)	-0.1197*** (3.19)
Loss		-0.2137*** (10.74)	-0.1197*** (8.31)
Class action litigation risk		-0.0311 (1.04)	-0.0227 (1.16)
Time Trend		-0.0227*** (3.86)	-0.0016 (0.28)
Firm fixed effects	No	No	Yes
N	18,045	18,045	18,045
R^2	0.0019	0.2547	0.8531

Notes: t-statistics in parentheses. *, **, and *** represent significance at the 10%, 5%, and 1% level, respectively.