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Governance and Payout Precommitment

Kose John, Anzhela Knyazeva, Diana Knyazeva

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Governance and Payout Precommitment***Kose John[†]**

New York University and Temple University

Anzhela Knyazeva

Securities and Exchange Commission

Diana Knyazeva

Securities and Exchange Commission

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Abstract

We examine how firms structure payout and debt commitments to address governance weaknesses. Firms with severe agency conflicts precommit through a combination of dividends and debt or through dividends rather than debt alone. Such firms also shift their shareholder payouts towards regular quarterly dividends – a stronger commitment than special dividends or repurchases. Although dividend commitments are implicit, event study evidence supports their credibility and value-relevance for firms with weak governance. Despite harsher penalties, debt alone cannot replace shareholder payouts as a means of addressing managerial agency conflicts.

JEL classification: G30, G34, G35, G32

Keywords: precommitment, payout, debt–dividend tradeoff, corporate governance

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[†] Corresponding author: Kose John, Stern School of Business, New York University, 44 West 4th St, New York, NY 10012. Phone: (212)998-0337. E-mail: kjohn@stern.nyu.edu.

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