



# Institutional Investors and Proxy Voting: The Impact of the 2003 Mutual Fund Voting Disclosure Regulation

Law Working Paper N° 83/2007

August 2007

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ECGI Working Paper Series in Law

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November 2018

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We have benefited from comments of Stanislav Dolgoplov, John Donohue, Peter Friz, Joy Ishii, Yair Listokin, Lynn Stout, Laura Starks, and participants at the Conference on Empirical Studies, ISNIE Annual Conference, NYU/Penn Conference on Law and Finance, University of Pennsylvania ILE Roundtable on Corporate Governance, and workshops at the law schools of the Universities of British Columbia, Illinois, Virginia, and at Yale School of Management. Dasol Kim provided excellent research assistance.

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## Abstract

This paper examines the impact on shareholder voting of the mutual fund voting disclosure regulation adopted by the SEC in 2003, using a paired sample of proposals submitted before and after the rule change. We focus on how voting outcomes relate to institutional ownership and the voting behavior of mutual funds. While voting support for management has decreased over time, there is no evidence that mutual funds' support for management declined after the rule change, as expected by advocates of disclosure. In fact, in the context of management-sponsored proposals on executive equity incentive compensation plans, mutual funds appear to have increased their support for management after the rule change. We also find that this result is not due to changes in compensation plan features, nor that voting outcomes were plausibly related to broker voting, which was eliminated in a parallel 2003 stock exchange rule change. Finally, there is some evidence that firms with greater mutual fund ownership adopt a higher frequency of sponsoring executive equity incentive compensation plans, which could partly explain our findings.

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Keywords: Proxy Voting, Mutual Funds, Institutional Investors, Disclosure

JEL Classifications: G34, G38, K22

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## 1. Introduction

The proxy voting process is a key mechanism by which shareholders monitor corporate managers. It is the means by which managers are replaced through proxy contests over director elections, and by which their major plans are reviewed as state law and stock exchange rules require shareholder approval of significant transactions. Moreover, in recent years, activist institutional investors have used the proxy process to advocate changes in corporate policies, such as repeal of takeover defenses and changes in board composition or managerial compensation. In January 2003, the U.S. Securities and Exchange Commission (SEC) required mutual funds to disclose how they voted on proxy proposals presented at shareholder meetings. This rule followed a series of significant federal government interventions into firms' corporate governance in the Sarbanes-Oxley Act (SOX), Congress' response to the scandals of 2001-2002 that began with the implosion of Enron. In this paper, we treat this disclosure rule change as a natural experiment to investigate how this affected mutual funds' voting behavior.

There is a substantial literature debating Congress' legislative product, both for SOX's substantive content and for jurisdictional overreaching into subject matters long considered to be the domain of state corporate law – the governance of public corporations (e.g., Bainbridge, 2003; Cunningham, 2003; Romano, 2005). The fund vote disclosure rule has, however, been the subject of only limited study. Yet this rule was also intended to affect public corporations' governance, albeit more indirectly than SOX, by rendering mutual funds more active monitors who would be less supportive of management, and the agency's proposal of the rule generated considerable industry opposition in contrast to the muting of opposition in the whirlwind of events accompanying the enactment of SOX.<sup>1</sup>

This paper examines the impact of the mutual fund voting disclosure rule on corporate governance by examining its effect on proxy voting outcomes. To this end, we construct a sample of firms that experienced similar proposals, sponsored either by management or shareholders, both before and after the 2003 rule change. We examine the difference in voting outcomes before relative to after this rule change, particularly in relation to mutual fund ownership, controlling for firm characteristics, including performance, non-mutual fund institutional ownership and governance features.

We find that voting support for management has been declining for close to a decade and that mutual funds appear to support management less frequently than other investors. However, we find no evidence that the rule decreased mutual funds' voting in support of management. Indeed, some of our results suggest that mutual funds' support for management increased after the rule's adoption, particularly for executive equity incentive compensation

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<sup>1</sup>As the SEC (2003) put it upon adopting the rule: “[R]equiring greater transparency of proxy voting by funds may encourage funds to become more engaged in corporate governance of issuers held in their portfolios, which may benefit all investors and not just fund shareholders.” The controversy over the rule's adoption is discussed in part 2.

plan (EEIC) proposals. This finding is contrary to the expectation of disclosure rule advocates, who contended that funds voted with management due to conflicts of interest and would reduce that support once their votes were transparent.

As the decision to put up an EEIC proposal is clearly a choice by management, we investigate to what extent selection issues could potentially explain our findings by comparing firm characteristics and outcomes to a matched sample of firms experiencing similar proposals solely before the disclosure rule change but not after. The main robust result here is that greater ownership (level and increase) by mutual funds is associated with a higher likelihood of firms' sponsoring an EEIC proposal after the rule change, which again is not consistent with the view that disclosure would result in increased opposition to management by mutual funds whose votes were conflicted and favored management when they were not revealed publicly. There is some evidence that firms with EEIC proposals after the rule change had higher profitability before the rule change, though this is only marginally significant, and the difference in profitability across the two samples is not significant after the rule change.

Finally, we find that some takeover defenses decrease support for management, results independent of the rule change, but the results are so varied across defenses, and within and across proposals, that we cannot draw a conclusion regarding the relation between defenses and voting outcomes.

The paper is structured as follows. Section 2 reviews the debate over the vote disclosure rule and the existing empirical research on institutional investors' potential conflicts of interest in voting. Section 3 introduces our research design and sample characteristics. The results of the analysis are discussed in detail in section 4. We begin by analyzing regressions in which we infer votes simply from institutional holdings. We then use funds' actual votes after the rule change to predict fund votes before the rule change, and use our estimate of the total fund vote in the regressions. Finally, for EEIC proposals, section 5 compares the results of the sample firms to a matched sample of firms that only offered proposals prior to the mutual fund vote disclosure rule. Section 6 concludes.

## **2. Conflict of interest concerns and the mutual fund proxy vote disclosure rule**

The requirement of mutual fund proxy vote disclosure was proposed by activist institutional investors who maintained that disclosure would reduce mutual fund managers' conflicts of interest (IRRC 2002; Teitelbaum 2003). Mutual fund managers were said to vote in support of corporate management, at the expense of investors in the funds, in order to facilitate other business relations with the corporations whose shares they owned. The rationale for the rule was that, once votes were revealed, investors could better monitor fund managers and thereby constrain such conflicts. Labor union funds were vigorous advocates of the rule change, having petitioned the SEC in 2000

and 2001 to require the disclosure (IRRC, 2002:1), as they considered it to be a key mechanism for monitoring whether mutual funds' voting meshed with union voting policies.<sup>2</sup>

The SEC's adoption of the vote disclosure regulation generated considerable controversy.<sup>3</sup> Members of the fund industry expressed concern that vote disclosure would lead to pressure and retaliation by corporate managers<sup>4</sup> and to politicization of the proxy process by organizations, such as labor unions, and social responsibility activists. The latter contention was that such organizations and activists, whose investment objective differed from other shareholders with regard to the maximization of share value, would engage in media campaigns against the funds' voting records. Mutual funds also objected that the cost of the disclosures would exceed the benefit to investors, noting that the vast majority of mutual fund holders never expressed interest in how funds voted. The SEC dismissed the industry's concerns and promulgated the disclosure rule, considering the benefit of transparency to outweigh the asserted costs.

Rothberg and Lilien (2006) and Davis and Kim (2007) both examine the premise of the advocates of the vote disclosure rule, namely, conflicted voting by mutual funds, by analyzing the mutual fund votes disclosed since adoption of the rule. Neither study finds evidence of conflicts of interest influencing fund voting.

Rothberg and Lilien (2006) investigate voting by the five largest mutual fund families on all proxy proposals, whether sponsored by management or shareholders. To examine the issue of conflicted voting, they compare the votes of the four large mutual funds whose business they consider to be "mostly mutual fund" companies (i.e., non-conflicted), with the votes of the one large fund that is affiliated with an insurance broker, and three additional financial services firms with mutual funds which they characterize as "mostly not mutual fund" companies (i.e., potentially conflicted because the funds' parents' business is principally the provision of financial services rather than the mutual fund business). The hypothesis is that if conflicts of interest lead funds to vote for management, then mutual funds with a sizeable amount of "non mutual fund" business should be more likely to vote in support of management than funds for whom other business opportunities are not a factor. Rothberg and Lilien find that there is no significant difference in the average support levels across the two sets of funds. They conclude, albeit tentatively because of the small sample size, that there is no evidence of conflicted voting by mutual funds.

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<sup>2</sup> With the rule's implementation they have indeed done so. In March 2006, for example, the AFL-CIO surveyed mutual fund voting and reported to the press that it found that the "top eight mutual funds [were] in the bottom tier with regard to voting in line with AFL-CIO proxy voting policies" (BNA, 2006:294).

<sup>3</sup> The SEC received over 8,000 comment letters in response to the proposed rule (the vast majority being form letters supporting the rule sent in response to an organized writing campaign by the groups advocating its adoption): labor unions, public pension funds and individual investors supported the proposed rule, while the fund industry overwhelmingly opposed it (SEC 2003).

<sup>4</sup> This was, in fact, the argument made in support of shareholder proposals to require confidential proxy voting sponsored by activist institutional investors in the late 1980s- mid 1990s (Romano, 2003).

Davis and Kim (2007) analyze mutual fund conflicted voting by examining the voting of mutual funds that manage corporate-sponsored pension plans. They compare mutual funds' voting on shareholder proposals at firms whose pension plans the funds manage with their votes at firms whose pensions they do not manage. Davis and Kim find that there is no significant difference in funds' voting support for management of clients and of non-client firms. An explanation they advance for the failure to find evidence of conflicted voting is that the funds knew that their votes were under scrutiny in the post-Enron environment that included mutual fund scandals involving discriminatory and illicit trading practices, and therefore they were constrained from voting differently for client and non-client firms, "even if that was the standard practice before" (Davis and Kim, 2007: 564). An alternative plausible interpretation of their data, consistent with Rothberg and Lilien's study, is that mutual funds' proxy voting is not affected by conflicts of interest.

Davis and Kim further investigate the question of conflicted voting at what they characterize as a fund's voting "policy level," by aggregating all of a mutual fund's votes to calculate an average support rate, independent of votes at client and non-client firms, and comparing those votes to those of the College Retirement Equity Fund (CREF) and the California Public Employees Retirement System (CalPERS), two activist institutional investors with no business ties. In this analysis, Davis and Kim find a significant negative relation between funds' number of clients and voting support, that is, the more pension plans a fund manages, the more likely it votes against shareholder proposals in general. In other words, funds with more business relations adopt voting policies that tend to support management, even if their specific votes do not differ for client and non-client firms.<sup>5</sup>

In sum, these two studies of mutual fund voting after the adoption of the vote disclosure rule offer differing assessments of mutual fund voting, although neither study identifies evidence of conflicted voting. Inferences from those studies are greatly hampered, however, by being limited to investigating voting subsequent to the rule change. If, as union funds contended in urging the SEC to adopt the rule change, disclosure eliminates conflicts of interest, then we would not expect to find evidence of a conflict in post-disclosure rule data. This is an explanation Davis and Kim advanced for their inability to identify differences in fund voting for clients and non-clients.

Therefore, to address that possibility, it is necessary to contrast voting outcomes both before and after mutual funds' votes had to be disclosed, which is the main strategy pursued in this paper. Because actual votes are,

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<sup>5</sup> Because the set of proposals voted on by the mutual funds and CREF and CalPERS is not identical, the support percentages are not necessarily comparable. For instance, if CREF voted on more defensive tactics and fewer compensation proposals than did a mutual fund, then with identical voting policies of supporting defenses and opposing compensation proposals, the two institutions' support level for management would differ in the direction Davis and Kim found. When Davis and Kim reanalyze the data by proposal type, the client variable is significantly negative only for some proposal categories, and it is insignificant for proposals to remove takeover defenses considered the most likely to decrease shareholder value. They conclude that funds are less likely to oppose



of course, not available prior to the 2003 adoption of the disclosure requirement, we combine the inferential approach based on relating voting outcomes to holdings by different investor groups (as used by earlier studies of conflicted voting<sup>6</sup>) with actual voting data, to examine changes in voting on both management and shareholder proposals before and after the adoption of the disclosure requirement.<sup>7</sup>

### 3. Sample construction and description

Our main analysis uses a sample of ‘proposal pairs,’ i.e. similar proxy proposals for the same firm, with one proposal submitted before, and the other after, the mutual fund vote disclose rule’s effective date of July 1<sup>st</sup>, 2003.<sup>8</sup> We construct our sample of pairs of proxy proposals from all votes on proxy proposals that are included in the Investor Responsibility Research Center’s (IRRC) database of proxy voting from 1994-2005 and that are classified by the IRRC as corporate governance (rather than social responsibility) proposals.<sup>9</sup> The IRRC tracks the proxy votes of over 1,900 firms, including the Fortune 500 and Standard & Poor’s 500 (covering fewer firms, however, in the earlier years). Using IRRC’s four digit coding of the subject of the proposals, we identify all firms that had a vote on a proposal with the same code before as well as after the date of the mutual fund vote disclosure

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management on proposals in “gray” areas regarding shareholder value (Davis and Kim, 2007: 565).

<sup>6</sup> In the late 1980s, when managements were seeking approval of takeover defenses, two studies examined whether institutional investors’ voting in that context was influenced by conflicts of interest, the focus then being on banks and insurance companies as the potentially conflicted shareholders. Brickley et al. (1988) found that support for managements’ defensive tactic proposals was positively correlated with the stockholdings of banks and insurance companies, and considered this evidence of conflicted voting (those institutions, in their view, being more sensitive to management pressure to vote for the proposals because they could have other business relations with firms). However, Van Nuys (1993), in a case study of a contested proxy solicitation by Honeywell management to adopt defensive tactics, tracked the actual votes of institutions and their business relations with the firm, and found, in contrast to Brickley et al.’s inference, that there was no significant difference in support level between financial institutions with business relations with Honeywell and those without such relations.

<sup>7</sup> We relate institutions’ reported holdings to voting, as is common in the literature, e.g., Brickley et al. (1988), but this approach will overstate their voting impact if they are engaged in substantial stock lending programs and do not recall their shares by the record date in order to vote them. Although for the sample proposals voted on after adoption of the disclosure rule we know that mutual funds voted in virtually all instances where share holdings were reported, we do not know whether they retained only a small percentage of their reported holdings to record a vote and lent out the majority of their shares, or voted all of their reported holdings, because the SEC does not require disclosure of the number of shares voted.

<sup>8</sup> The rule’s effective date was actually April 14, 2003, but mutual funds were not required to disclose votes cast before July 1, 2003. We therefore refer to the July date as the rule’s effective date, as it is the relevant date for purposes of analysis. Because very few firms hold annual meetings from May-June (meetings coincide with the release of annual financials in the first quarter following the close of the firm’s fiscal year, which ends, for the vast majority of firms, on December 31, or, to a lesser extent, June 30), the difference between the rule and reporting effective dates of April and July 2003 made virtually no difference regarding what votes cast in 2003 had to be disclosed. Note that there is a lag between a vote and its disclosure under the rule: funds have to file voting reports by August 31 for votes cast during the previous 12 month period running from July 1 – June 30 (that is, the first reports under the rule were filed in August 2004, for votes cast from July 1, 2003 – June 30, 2004).

<sup>9</sup> Social responsibility proposals are not intended to affect corporate performance, and the conflicted voting concern is, accordingly, not implicated by voting on such proposals, because a vote for management, even if motivated by furthering business relations, would not be a vote contrary to the funds’ investors’ interest.

rule's effective date (i.e., meetings held after June 30, 2003). To minimize changes in a firm's environment, we adopt the following matching rule: When there is a choice, we include the proposal voted on at the last meeting occurring before, and at the first meeting occurring after, the disclosure rule's effective date. As indicated in Table 1, this produced 1,006 proposal pairs (2,012 proposals), offered at 680 firms. After eliminating proposals for which key data were missing (e.g., voting outcomes from IRRC or accounting performance measures from Compustat) and those proposed at firms with dual class stock,<sup>10</sup> the sample consists of 853 proposal pairs offered at 582 firms.

Information describing the sample proposals and firm characteristics is included in Tables 2-3. As indicated in Table 2, slightly over 80 percent of the proposals are sponsored by management, with the largest category involving approval of compensation plans (69 percent). Of the shareholder proposals, the largest category (half) concerns removal of takeover defenses. Because proposals grouped into the management compensation category are diverse, we divide them into four subcategories: (i) EEIC proposals; (ii) outside directors' equity incentive compensation plan proposals; (iii) employee stock purchase plan proposals; and (iv) bonus plan proposals.<sup>11</sup> The table illustrates the well-known relationship that outcomes differ dramatically by proposal type. Management proposals receive considerably more support than shareholder proposals; and among management proposals, EEIC proposals have lower average support levels. In addition, shareholder proposals on takeover defenses receive far greater support than shareholder proposals on executive compensation or board independence.

Table 2 also presents voting outcomes by proposal type, separately calculated for proposals voted upon before and after the adoption of the mutual fund vote disclosure rule. For most proposal categories, the voting support for management's position declined after the rule change, and the difference is statistically significant. These striking univariate statistics are our focus of inquiry. Our analysis seeks to determine whether increased opposition to management is attributable to the disclosure rule, and thereby indirectly whether the rule reduced conflicted voting by mutual funds, as the SEC and the rule's advocates anticipated. Because firm-specific factors and proposal features may affect voting outcomes, we control for such variables in the analysis as data availability allows.

Table 3 provides descriptive statistics for the sample firms, including characteristics that other studies have found to be relevant to voting outcomes, such as institutional ownership and profitability (e.g., Gillan and Starks,

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<sup>10</sup> Proposals offered at firms with dual class stock were eliminated from the sample to ensure that institutional ownership accurately measures institutions' voting rights. These deleted proposals were approximately 20 percent of the original population of matched pairs. We also eliminated proposal pairs of firms with missing accounting performance data, insufficient data to calculate market betas and those for which Thomson Financial Services' database of institutional investor holdings computed the institutions' share as over 120 percent.

<sup>11</sup> Table 2 indicates the IRRC classification codes defining the subcategories. We also analyzed the data aggregating the equity incentive compensation proposals for executives and outside directors (codes 1500-49), and the results are

2000; Thomas and Martin, 2000). The table also presents mean values of firm characteristics for two alternative cuts of the data, grouped by whether the proposal was a management or shareholder proposal, and grouped by whether it was submitted before or after the disclosure rule's adoption.

We obtain the percentage of outstanding shares owned by each of five institutional investor classes from Thomson Financial Services.<sup>12</sup> Ownership of directors (separately classified for independent directors and insiders) is obtained from the IRRC's directors database.<sup>13</sup> We collect additional firm-specific variables that are typically correlated with institutional ownership, for use as further proxies for institutional ownership (small institutions are not subject to the SEC reporting requirements) and as controls: market capitalization and share turnover from CRSP.<sup>14</sup> Several performance measures commonly used in the literature are taken from CRSP and Compustat: past stock and market returns calculated over the 12-month interval prior to the date of the meeting at which the proposal is offered, return on assets (ROA), and net profit margin (NPM).<sup>15</sup>

The main explanatory firm-level characteristics that have been used in the proxy proposal literature are performance and ownership. An extensive literature has developed (after the bulk of the research on proxy proposals was undertaken) on the relation between performance and governance structure, although whether a true (causal) relation has been identified is in dispute (e.g., Gompers et al. 2003; Lehn et al. 2007). Because corporate governance is of significant concern to many institutional investors, particularly activist institutions which are likely to sponsor shareholder proposals, the presence or absence of governance devices those investors deem important could affect voting outcomes, independent of whether they affect performance.<sup>16</sup> We therefore include in our analysis of proxy

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similar to, but noisier than, those reported for the analysis of only EEIC proposals.

<sup>12</sup> Institutional investment managers with discretion over accounts of at least \$100 million must report their holdings to the SEC quarterly on form 13-f. Thomson collects data from 13-f filings and sorts the reporting institutions into five classes: (1) banks (2) insurance companies; (3) mutual funds and their advisors; (4) independent investment advisors; and (5) others, which includes public pension funds and university endowments. If the Thomson data produced institutional holdings that summed to over 100 percent but less than 120 percent (58 observations), we rescaled the institutional holdings by the sum total. We take account of classification errors in the Thomson database whereby institutional classifications after 1998 of institutions previously included in the database were all erroneously set to category 5. We correct for this data error by classifying those institutions according to their pre-1998 category for years after 1998. Following Brickley et al. (1988), classes 1 and 2 are combined - these institutions may have conflicts (the rationale for their approach) but are not subject to the disclosure rule. Our results are robust to retaining these as separate classes or combining all classes but the class affected by the rule.

<sup>13</sup> The IRRC collects these data from firms' SEC proxy filings. This database is much smaller than IRRC's voting database. As a consequence, we lose approximately half of our sample observations when the director ownership data are used in the analysis. Moreover, because for many pairs IRRC data exist only for either the 'before' or the 'after' proposal, the usable dataset is far smaller than that implied by the number of observations. The descriptive statistics for those variables in Table 3 are calculated using only the 420 observations comprising pairs where the data are available for both the 'before' and 'after' proposal.

<sup>14</sup> Bethel and Gillan (2002) find that turnover from record to meeting date is positively related with voting support for management.

<sup>15</sup> Values of ROA or NPM below -1 are truncated to -1. We also calculated past stock returns using 24- and 60-month intervals, return on equity, and industry-adjusted ROA and NPM, and the results are unchanged.

<sup>16</sup> The websites of leading institutional activists, such as CalPERS and the AFL-CIO, focus on good corporate

voting, firms' governance features related to takeover defenses and board structure.

Five governance features related to takeovers are used in our analysis: the presence of a poison pill and the four individual charter and by-law provisions comprising the parsimonious takeover defense index constructed by Cremers and Nair (2005), which is a subindex of the G index created by Gompers et al.(2003): ability to issue blank check preferred stock; the presence of a staggered board; restrictions on shareholders' ability to call special meetings; and restrictions on shareholder action by non-unanimous written consent. For the many sample observations that are not in the IRRC's governance database, the source for these data, we hand collect the information from firms' SEC filings.

For governance features related to board structure, we collect from the IRRC's director database board size and composition (percentage of independent directors), in addition to the stock ownership of directors mentioned earlier.<sup>17</sup> These are mechanisms of corporate governance well-recognized in the literature on governance and performance, and included in other governance indices (e.g., Brown and Caylor 2006). For example, Yermack (1996) finds an inverse correlation between performance and board size. Independent directors' ownership has also been found to correlate positively with performance (Bhagat and Bolton 2006). Although the literature does not find that increased board independence improves performance (Romano 2001:191-95), independent directors are emphasized in activist institutions' lists of good governance practices (e.g., Council of Institutional Investors 2006), and are a focal point of both federal and state regulation of corporations.

Table 3 shows that the same characteristics are present in the subsamples (of management versus shareholder proposals) as in the full sample: high institutional ownership, numerous takeover defenses, independent boards, and low director stock ownership. Moreover, sample firms receiving shareholder proposals are similar to those in other studies of shareholder proposals.<sup>18</sup> The average length of time between the 'before' and 'after' proposals for the same firm is about 3.4 years, and slightly longer for management proposals.<sup>19</sup>

#### **4. Results**

Our main analysis seeks to explore whether mutual funds changed their votes after the disclose regulation

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governance practices, as does the Council of Institutional Investors' (CII) website.

<sup>17</sup> The IRRC directors' database contains information on more firms' board composition than director ownership, and we thus lose only about 30 percent of the sample observations when board variables are included in the analysis.

<sup>18</sup> For example, comparing the mean characteristics of the shareholder proposal firms to those in Thomas and Cotter's (2007) study of shareholder proposals from 2002-04, the mean institutional holdings are similar: 68 percent compared to 67 percent, respectively. Our firms are slightly less profitable: mean return on assets of 3 percent compared to 4 percent, respectively and net profit margin of 5.6 percent compared to 6.2 percent, respectively. They are also somewhat smaller, with respective mean market capitalizations of \$37 billion and \$43 billion.

<sup>19</sup> We find that the length of time between 'before' and 'after' proposals is not related to the aggregate voting

came into effect on July 1, 2003. As we do not observe their vote before, we first investigate the aggregate voting outcome and its association with mutual fund holdings, and whether there is any difference for proposals before versus after the disclosure rule took effect, controlling for other characteristics (including, for EEIC proposals, more detailed features of the proposals themselves, where data are available). We then use the actual disclosed mutual fund votes for the ‘after’ proposals to estimate the total mutual fund vote for each proposal based on firm and fund characteristics, and again, look for evidence that its association with the aggregate voting outcome changes before versus after the rule change.

Our main dependent variable is the aggregate vote in support of management and shareholder proposals (where a vote for a shareholder proposal is a vote against management, because in virtually all cases management took a position against the proposal). As the percentage of votes ranges between 0 and 1, it is transformed by a logistical transformation,  $\log [\text{percentage of votes for}/(100 - \text{percentage of votes for})]$ , to create a continuous variable with negative as well as positive values, for ordinary least squares estimation. As voting outcomes differ by proposal type, we estimate separate regressions for each proposal category.<sup>20</sup>

If institutions vote differently from other investors, as a group, we would expect to find a relationship between voting outcomes and institutional ownership. In addition, by comparing the association between mutual fund holdings and voting outcomes before and after July 1, 2003, we can relate the impact of the rule change to change in those institutions’ voting. We use aggregate holdings of four classes of institutional investors: banks and insurance companies; mutual funds, the affected class; independent investment advisors; and the remainder other institutions category that includes, among others, activist investors such as public pension funds and hedge funds.

Given our interest in the effect of the mutual fund vote disclosure rule, we include a dummy variable (“after”) to indicate whether a proposal was introduced before or after the rule’s effective date, and interact the principal independent variables of interest with that ‘after’ dummy. The interactions of the ‘after’ dummy with institutional holdings are thus intended to capture changes in aggregate voting before versus after the disclosure rule. As only one class of institutions, mutual funds, was subject to the rule, we would expect a change only for this group. If all classes of institutional investors experienced a similar change, then we would not be able to attribute a change in mutual funds’ voting to the disclosure rule. The principal regression model estimated is:

$$\ln [\text{votes}_{for}/(100-\text{votes}_{for})] = \alpha + \beta_1 \text{After} + \beta_{2..k} \text{Controls}(\text{size}, \text{profitability}, \text{governance})$$

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outcome (results not reported).

<sup>20</sup> Proposal categories with too few observations to be estimated reliably are omitted from the analysis. Deleted proposal categories (with the number of pairs in parentheses) are, for management proposals: outside director equity incentive compensation plans (36), removal of defenses (3), mergers (1), and miscellaneous (10); and for shareholder proposals: board independence (18), director elections (1), and miscellaneous (14).

$$+ \beta_{k+1\dots m}(\text{institutional ownership}) + \beta_{m+1\dots n}(\text{After* institutional ownership}) + \varepsilon.$$

All regressions are estimated using ordinary least squares and robust standard errors after Huber and White. Tables 4 and 5 contain the analysis of EEIC proposals and of all other proposals, respectively. Our primary focus will be on the interaction of mutual fund holdings with the ‘after’ dummy, in order to see whether there is any effect of the vote disclosure rule change.

#### **4.1. EEIC proposals**

EEIC proposals are both the most controversial proposals sponsored by management, as indicated by their overall lower voting support, and the most frequently occurring (given our chosen categories). Therefore, they are the main focus of our attention, with the results reported in Table 4. We first consider the level of the aggregate voting outcomes before and after the disclosure rule change and its relationship with mutual fund holdings and firm governance and performance (panel A of Table 4). Next, we control for detailed plan features that are available for a subset of the EEIC proposals (panel B).

##### **A. Votes before and after, basic results**

The first key finding is a marginally significant negative relation between mutual funds’ holdings and voting outcomes unconditionally, but a marginally significant positive interaction term of mutual fund holdings with the ‘after’ dummy (see the first column of Table 4, panel A). Moreover, the net effect after the rule change is positive, such that proposals at firms with more mutual fund ownership afterwards had more support. While the latter net effect is not statistically significant, these results clearly do not sustain advocates’ expected view of the benefits of the rule change because, if their analysis were correct, we should find a decrease in mutual funds’ support for management after the rule (under the rule’s advocates’ perception that prior to the rule funds engaged in conflicted voting, and that disclosure would diminish such activity). Yet any conclusion to be drawn from the data would be the opposite, namely that mutual funds increased their support for management after adoption of the rule. In this respect, the data could be characterized as lending support to the view of advocates of confidential voting, that transparency subjects institutions to management pressure to support its position, rather than the view of vote disclosure rule proponents.

We do not find any significant relation for the other three categories of institutional holdings, which were not directly affected by the rule change and which is thus as expected. That finding bolsters the conclusion that the mutual fund holding results are attributable to the rule and not to some other overall change in the proxy voting

environment. We find several distinctive results regarding the relation between the control firm characteristics and voting outcomes independent of the rule change. First, the EEIC proposals fare better in larger firms (i.e., support is positively associated with the firm's market capitalization) and worse in firms with higher stock turnover. In addition, performance is not a significant factor in voting support, as stock market performance is insignificant, ROA is negative but NPM is positive and the net effect insignificant. The performance finding is in contrast to Thomas and Martin (2000), who report a negative relation between performance and voting support, but parallels a finding of no significant relation by Morgan et al. (2006).<sup>21</sup> For the defenses, only the presence of a poison pill is significantly negatively related to voting outcomes; the other defenses are insignificant. This may reflect shareholder dissatisfaction with, or hostility to, managers who have adopted what is considered by many commentators the most potent defensive tactic. Because we control for accounting and stock market performance, the negative significance of poison pills does not seem to be a marker for poor performers adopting the defense and shareholders voting against management due to poor performance.<sup>22</sup> Finally, confidential voting does not appear to be a factor: the presence of confidential voting is insignificant in our base model (column 1 in panel A of Table 4).<sup>23</sup>

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<sup>21</sup> A joint test of the significance of the three performance variables is also insignificant (F statistic of 1.6, p-value of .2). The difference in our results with Thomas and Martin may be due to differences across samples or the performance measure. We only consider firms with EEIC proposals offered both before and after July 1, 2003, while their sample consists of proposals in 1998. We think the difference in the sample rather than profit measure is the more likely explanation because the Morgan et al. study's sample period, consisting of plans proposed over 1992-2003, is more similar to ours, while they use the same profit measure as Thomas and Martin, market-adjusted prior stock returns. Including all three firm-specific performance measures, past stock returns, NPM and ROA, as well as the past return on the market does not present collinearity problems in the reported regressions: variance inflation factors (VIFs) are all less than 10 (see Chatterjee and Hadj, 2006: 236-238). In unreported regressions we also interacted the profitability variables with the 'after' dummy; none of the interactions are significant.

<sup>22</sup> As a further check, we interact the presence of a poison pill with our performance measures, none of which are significant, while for some estimations of EEIC proposals, the interaction terms of poison pills with the accounting variables are marginally significant and opposing in sign (positive for ROA and negative for NPM). Overall, this suggests that the presence of the poison pill defense reduces support for management independent of performance. We also interact the presence of a poison pill with the 'after' dummy, and find that it is insignificant. Interactions are also insignificant for blank check preferred stock, classified boards, and restrictions on shareholder meetings but significantly negative for restrictions on written consents. If that interaction term is further interacted with mutual fund holdings, then both interaction terms are insignificant but the interaction with poison pill becomes significantly negative. Finally, interacting poison pills, mutual fund holdings and the 'after' dummy, the triple interaction is significantly positive, the single interaction between the defense and 'after' is significantly negative while the single interaction between fund holdings and 'after' becomes insignificant. This might suggest that post-rule mutual funds' votes are affected by governance mechanisms, and that they increased their support for EEIC proposals in the presence of a poison pill, a counterintuitive result. But if the straight interaction with fund holdings and poison pills is also included, that term is significantly positive and the triple interaction term with the 'after' dummy is not. A possible interpretation is that funds consider performance pay more important when management is entrenched against takeovers, which should be independent of the rule change, as indicated by the last-mentioned result.

<sup>23</sup> It is significantly negative in some model specifications in the subset of EEIC proposals for which we have board data (e.g., column 2 of the panel). The presence of confidential voting was included as a control because its proponents contend that it reduces conflicted voting, despite an absence of supporting data (see Romano, 2003). Mutual funds' votes on proposals in firms with confidential voting became newly revealed to management after the rule change, along with their disclosure to investors and members of the public, whereas managers of firms without confidential voting could identify how mutual funds voted prior to the rule change. We therefore also examined interaction terms with the presence of confidential voting to take account of its potential impact on voting outcomes

## B. Board characteristics

We next explore whether board characteristics affect outcomes, and in particular, mutual fund behavior in relation to the rule change. The category of EEIC proposals is the only one for which we have sufficient information on board composition and ownership to undertake a statistical analysis.<sup>24</sup> The subsample of proposals for which we have board data is similar to the full set of EEIC proposals for the key firm characteristics of interest.<sup>25</sup>

Column 2 (Panel A, Table 4) reports the regression results when the four board governance variables are added (insider and independent director holdings, board size and board independence) with triple interactions of these governance variables with mutual fund holdings and the ‘after’ dummy. There is one critical finding: the triple interaction term between mutual fund holdings, independent director holdings, and the ‘after’ dummy is significantly positive. Further, once these triple interactions are included, mutual fund holdings by themselves or interacted with the ‘after’ dummy (but not interacted with independent director holdings) become insignificant.<sup>26</sup> In other words, mutual funds increase their support for management-sponsored EEIC proposals after the rule change at firms where independent directors hold more shares.

This suggests that the previous results of increased support after the disclosure rule’s adoption by mutual funds for management’s executive compensation packages depends upon other governance mechanisms in place.<sup>27</sup> In particular, mutual funds may use independent director ownership as a factor for supporting management when their votes are publicly disclosed, at least in the context of controversial proposals such as executive incentive compensation. This further suggests, in contrast to the results regarding confidential voting, that mutual funds may

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changing after the rule. This interaction of the ‘after’ dummy and confidential voting is insignificant if added to the reported regression. In addition, neither the interaction of mutual fund holdings with confidential voting, nor the triple interaction of mutual fund holdings, confidential voting and the ‘after’ dummy, was significant (unreported).

<sup>24</sup> There are 129 pairs of EEIC proposals that have board data for both the ‘before’ and ‘after’ proposal. The number of pairs with board data for both ‘before’ and ‘after’ proposals in the other categories of manager and shareholder proposals analyzed in Tables 5 ranges from 3 to 25.

<sup>25</sup> The firms for which board data are missing are larger and have greater accounting profitability, but the key variable of interest, mutual fund ownership is indistinguishable (respective means of 17.6 and 17.9 percent). There is also no difference in ownership of banks and insurance companies and the other institutions category; however, the board subsample firms have significantly lower ownership by independent investment advisors (23 versus 25 percent). Finally, there is no difference in the rate at which these firms have takeover defenses or confidential voting.

<sup>26</sup> If added, the interactions of the governance variables with the ‘after’ dummy itself are not significant and do not affect results. Also, the results for the specification of column 1 for the smaller sample where board variables are available are very similar to the results of the larger sample. In addition, if the interaction terms with poison pills are included in the regression (see note 22), the triple interaction between fund holdings, independent directors’ stockholdings and the ‘after’ dummy remains significantly positive, along with the interaction between poison pills and fund holdings while the triple interaction between pills, holdings and ‘after’ is insignificant.

<sup>27</sup> The significance of the interaction term is not due to the shares voted by the independent directors (whose average holding is 0.65 percent, with a range of 0 to 14.6 percent): we control separately for the directors’ ownership and that variable is insignificant if interaction terms are included (and only marginally significant without interactions).



not be completely indifferent to the transparency of the voting environment.

Why would independent director ownership impact the voting on management compensation proposals by mutual funds? One explanation is suggested by the finding in the literature that such directors' ownership is positively correlated with performance (Bhagat and Bolton 2006). That finding may be explained by directors with higher ownership being better monitors (and/or advisors) of management. Such directors may also be more likely to scrutinize managements' compensation and hence, their firms would be more apt to introduce value-maximizing plans. The increased support associated with higher mutual fund holdings in that scenario would be due to plans offered by companies with independent directors with higher ownership having fewer terms deemed unfavorable by shareholders.<sup>28</sup> However, because one might expect voting in favor of such higher quality compensation plans to be independent of the 2003 adoption of the vote disclosure rule, that alternative is not a fully satisfactory explanation of the significance of the three-way interaction term.

An alternative hypothesis that better explains the result is that mutual funds began to key on outside directors' ownership, as a signal of compensation plan quality or as a defensive strategy, given the disclosure of their votes, when supporting proposals that had become increasingly controversial in the post-Enron environment of the vote disclosure period. We investigate this alternative explanation of the data by interacting independent director ownership and the 'after' dummy with the holdings of the other classes of institutional investors. As column 3 (panel A, Table 4) indicates, we find the same significant, positive triple interaction term for independent investment advisors as for mutual funds and their advisors, but a significant negative triple interaction term for other institutions, the institutional class including investor activists such as public pension funds and hedge funds.<sup>29</sup> The interaction term for banks and insurance companies (institutions characterized as conflicted in the confidential voting literature but unaffected by the disclosure rule) is insignificant. This suggests that the finding for mutual funds is distinctive among voters with potential conflicts, and accordingly, offers some support for the interpretation that funds began keying on outside director ownership when their votes became disclosed.<sup>30</sup> Whichever explanation

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<sup>28</sup> We discuss the effect of changes in plan features on voting outcomes in part 4.1.D. For the subset of firms for which we have both director ownership and plan features (depending on the plan feature, ranging from 49 to 78 pairs of proposals), the correlations between independent director ownership and the presence of plan features institutional investors consider undesirable are mostly negative (ranging between -.05 and -.12), consistent with the hypothesis in the text, but none of the correlations are statistically significant (whether computed for the full sample or for only the 'before' or 'after' sets of proposals).

<sup>29</sup> The 'after' dummy and its interaction with other institutions' holdings are omitted from the regression because VIF tests indicate multicollinearity problems with their inclusion.

<sup>30</sup> If we combine all non mutual-fund institutions' holdings into one variable, as a further robustness check regarding our results for mutual funds, the three-way interaction term with independent director ownership and the 'after' dummy is negatively signed and insignificant. We do not emphasize this regression because it obscures different effects for different types of institutional investors. The result regarding the interaction terms with poison pills reported in note 26 supports this hypothesized explanation, as funds might be concerned that activist investors would

is thought to be more persuasive – higher independent director ownership being associated with proposal quality or funds’ desire to key on a governance feature post-vote disclosure – the finding is contrary to the expectations of advocates of the impact of the disclosure rule. For it is evidence that voting support for management by mutual funds did not decline after the rule’s adoption, but rather increased for that subset of firm proposals - management’s own equity incentive pay - that is most often criticized in the media and by activist investors.

### **C. The enactment of SOX**

Because incentive compensation came under increasing scrutiny and challenge by activist investors post-Enron, the ‘after’ dummy could be picking up changes in the proxy environment following the enactment of SOX, and not the impact of the mutual fund vote disclosure rule. We therefore estimate the regressions using an additional “after-SOX” dummy (post-July 2002) and report the results in columns 4 and 5 (panel A of Table 4). When only ‘after-SOX’ interactions are used for each class of institution (column 4), none of the interactions are significant. When we interact the institutional holdings variables with both the ‘after’ and ‘after-SOX’ variables (column 5), the ‘after’ interaction with mutual fund holdings remains marginally positively significant while all of the other interactions, particularly the ‘after-SOX’ interactions, are insignificant.<sup>31</sup> While anecdotal accounts suggest that the proxy environment for incentive compensation plan proposals became increasingly more difficult before the mutual fund vote disclosure rule was enacted, these results suggest that the effect on voting that our estimations capture is associated with the time frame of the rule’s adoption and not SOX.<sup>32</sup>

### **D. Compensation plan features**

Changes in compensation plan features over time are another potential alternative explanation of our results. In a study of EEIC proposals offered in 1998, Thomas and Martin (2000) identify five characteristics of compensation plans that are negatively correlated with voting support: dilution proportion (dilution caused by the specific proposal), total dilution (dilution due to all compensation plans and not just the plan under consideration), ability to reprice or exchange underwater stock options; extension of loans to exercise options; and awards of time-

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not accept the underlying incentive rationale for increasing support for EEIC proposals in the presence of a poison pill. A parallel explanation for the finding of increased fund support post-rule in conjunction with independent director ownership could be that ISS recommendations are more likely to be favorable in firms with higher independent director ownership. Independent director ownership is a positive factor in ISS’ corporate governance ratings. We could not test this alternative hypothesis, however, because ISS would not provide us with its recommendations for the sample proposals.

<sup>31</sup> VIFs indicate collinearity problems when both the ‘after’ and the ‘after-SOX’ interactions are included, however.

<sup>32</sup> We also tried adding a time trend, which is insignificant, indicating that our findings do not seem to be a function of a general temporal decline in support. Results are available upon request.

lapsing (non-performance-based) restricted stock. As they discuss, those features are known to be considered objectionable by institutional investors. In addition, a study of EEIC proposals introduced from 1992-2003 by Morgan et al. (2006) finds both dilution proportion and total dilution are negatively related with voting support. We are able to obtain information regarding at least one of the five undesirable plan features identified by Thomas and Martin for 258 EEIC proposal pairs.<sup>33</sup>

Table 3 reports summary statistics for the plan features, showing that there is no significant difference in dilution (proportion or total) across proposals offered before and after the mutual fund vote disclosure rule's adoption. There is a significant difference in the other three characteristics: significantly fewer plans permit repricing or loans, while significantly more plans award restricted stock post-disclosure. However, these changes cannot plausibly be related to management responding to the mutual fund vote disclosure rule. The reduction in repricing and loan provisions, which would be expected to increase support for the plans, can be attributed, respectively, to an alteration in the accounting rule for option repricing that imposed unfavorable financial statement treatment of such action (effective in 2001), and to SOX's prohibition of executive loans (e.g., Personick, 2005). The increase in restricted stock usage, which would be expected to decrease support, can be attributed to the change in accounting rule, announced in 2003 with a 2005 implementation date, to require option expensing, because that meant that firms no longer obtained an accounting "benefit" from option awards, and once the accounting treatment was equalized, restricted stock has other benefits compared to options, such as the award retains some value in market downturns (compared to options that become underwater), to make it preferred by managers and firms (e.g., Personick, 2005:8). Because the changes in plan features go in offsetting directions relative to institutional investor preferences, the overall decline in support for these proposals after 2003 cannot be straightforwardly attributed to changes in compensation plan features.

The results of adding plan features are in Panel B of Table 4. As indicated in column 1, dilution proportion, total dilution and the repricing dummy are significantly negative.<sup>34</sup> These results, which are consistent with those of Thomas and Martin (2000) and Morgan et al. (2006), suggest that the findings regarding fund holdings in the prior panel regressions are not due to changes in the compensation plans, because two of the three plan features that

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<sup>33</sup> We would like to thank Randall Thomas and Kenneth Martin for generously sharing with us their 1998 data. We use IRRC's online voting database for plan features, rather than collect and characterize plan features ourselves, in order to assure consistent treatment with plan classifications in the Thomas and Randall study, which are taken from IRRC data. Because the online IRRC database begins in 2001 and does not always summarize all features of plans in its analyses of proposals, we were able to obtain information on all five features for only 155 proposal pairs.

<sup>34</sup> Variables significant in panel A (size, poison pill) are no longer significant, nor are the mutual fund holdings variables marginally significant, but it should be noted that the number of observations is significantly reduced (310 or 342, depending on the model, compared to 816). In this reduced sample, the specification without plan features also renders the mutual fund holdings insignificant.

changed over time are not significantly related to the voting outcomes, and the one that is significant, the repricing dummy, is negative, while the number of plans permitting repricing declined after 2003. Interacting the plan variables with the ‘after’ dummy, only the total dilution interaction term is significant (column 2): while average total dilution is unchanged over the time period, after the disclosure rule proposals effecting higher total dilution attract more no votes.<sup>35</sup>

Next, we add interactions between the plan variables, mutual fund holdings and the ‘after’ dummy, while eliminating the interactions between plan features and the ‘after’ dummy that are insignificant, in order to determine whether the afore-mentioned effect is due to the rule change (i.e., due to a change in mutual fund behavior). None are significant (column 3). The results suggest that changes in plan features in the period following the disclosure rule’s adoption do not explain our other results, and that mutual funds have not reassessed their voting strategies for compensation plans post-disclosure.

#### **D. Broker nonvotes**

At the same time as the mutual fund vote disclosure rule was adopted, there was a parallel change in the proxy voting environment: the New York Stock Exchange (NYSE) altered its rule on when brokers can vote shares where the beneficial owner does not provide voting instructions so as to exclude all EEIC proposals effective July 1, 2003. The previous rule permitted broker votes on plans whose dilution proportion was under 5 percent. Bethel and Gillan (2002) find that under the prior regime, compensation plans received significantly higher support when brokers could vote. Of course, brokers could only vote on plans with low dilution levels, which would render the plans less objectionable to institutional investors and thereby attract more support independent of the broker votes. Nevertheless, it is possible that the inability of brokers to vote shares for all compensation proposals after the disclosure rule, compared to only some such proposals before its adoption, could confound the analysis of the impact of the mutual fund vote disclosure rule.<sup>36</sup> We therefore create a dummy variable indicating whether a plan’s

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<sup>35</sup> Because the restricted stock and loan dummies are insignificant, they are omitted from subsequent estimations, resulting in an increase in the number of observations. The regression reported in column 2 of panel B excludes the ‘after’ dummy and its interaction with other holdings, along with total dilution, because VIF tests indicate multicollinearity. If the interaction between the ‘after’ dummy and total dilution is excluded rather than total dilution, total dilution is significantly negative and the other results are unchanged. Morgan et al. (2006) find that the impact on voting outcomes of proposals’ dilution proportion declines over time; although their sample ends in 2003, that finding is consistent with our finding that the interaction between dilution proportion and the ‘after’ dummy is insignificant.

<sup>36</sup> The concern would be that an apparent increase in mutual fund support after the disclosure rule could be an artifact of the combination of a decline in non-institutions’ voting support (due to the loss of broker votes) and constant fund holdings. Gillan and Bethel’s analysis of the broker vote rule would predict a significantly negative ‘after’ dummy: voting support should decrease after the rule change with the elimination of brokers’ pro-management votes. However, the firms in Bethel and Gillan’s sample paid significantly lower proxy solicitation fees

dilution proportion is less than 5 percent. If managers had been proposing plans with dilution rates below 5 percent before 2003 to avoid the NYSE rule on broker nonvotes as Bethel and Gillan (2002:33) hypothesize, then we would expect the proportion of such proposals to decrease after the rule change because all plans now require a vote.

There is, however, no significant difference between the rate of dilution proposals above and below 5 percent, before and after July 1, 2003 (the mean value of the dilution dummy is .67 before and .62 after, with a t-statistic for the difference in mean of 1.0). In addition, when we include that dummy variable, and its interaction with the ‘after’ dummy in the full model regression including institutional investor variables along with the two other significant plan features, total dilution and repricing (plan features to which institutions object but that are not related to the broker voting rule), the ‘dilution’ dummy is significantly positive, while the ‘after’ interaction is insignificant (column 4, panel B of Table 4). There is greater voting support for proposals with lower dilution rates, and the broker voting rule change did not significantly alter that effect. We therefore believe that our previously-reported results regarding the interaction between the ‘after’ dummy, mutual funds and independent director stock ownership, are due to the vote disclosure rule and not the NYSE’s broker vote rule change.<sup>37</sup>

#### **4.2. Other management and shareholder-sponsored proposals**

In contrast to EEIC proposals, there is no relation between mutual fund holdings and the vote disclosure rule for the voting outcomes of any of the other categories of management-sponsored proposals or for shareholder-sponsored proposals. The results of analyses of the aggregate voting outcomes of these other types of proposals are reported in Table 5 and briefly summarized below.

##### **A. Employee stock purchase plans**

Management proposals on employee stock purchase plans receive much greater overall support than EEIC

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for proposals on which brokers could vote (they appeared to spend more on controversial proposals, on which brokers were not permitted to vote, such as shareholder proposals). It is therefore possible that management could maintain voting support levels for those proposals once broker votes are not permitted by increasing proxy solicitation expenditures. If that were the case, then the ‘after’ dummy would not be expected to be significant, as is the case in the regressions in panel A. Of course, that would also mean that the change in broker voting was ineffective from its proponents’ perspective, as it would have no impact on voting outcomes.

<sup>37</sup> As a final robustness check we reanalyze the voting outcomes by making use of the paired proposal structure with a differencing approach that examines the change in voting outcomes from the ‘before’ to the ‘after’ proposals’ dates. The results, available upon request, indicate that when the data are collapsed to use the difference in proposal pairs’ voting outcomes as the dependent variable, if the statistical significance of a regressor was only marginal in the original formulation, it is no longer significant, but if the statistical significance was at least 5 percent in the original formulation than that result is robust (i.e., the interaction of mutual fund holdings with the ‘after’ dummy becomes insignificant while the triple interaction with independent director holdings remains significant). More generally, we again find no evidence for the hypothesis of the advocates for the vote disclosure rule that mutual funds would lower their support for management when their votes were disclosed, and some evidence for the

proposals. Table 2 indicated that this support seemed to have declined in the period after the rule change, but the ‘after’ dummy is, in fact, significantly positive, suggesting the opposite, that support increased rather than declined post-rule (see column 1 of Table 5). The change in support cannot be directly connected to the mutual fund vote disclosure rule, however. As illustrated in column 1 of Table 5, the mutual fund ownership variables are insignificant. It seems that banks and insurance companies could be the source of the decline suggested by Table 2, although the interaction term is only marginally significantly negative. Pound (1988) and Brickley et al. (1988) have emphasized the potential conflicts of banks and insurance companies in proxy voting, but those institutions were unaffected by the vote disclosure rule.. Moreover, not being subject to the SEC’s regulatory authority,<sup>38</sup> those institutions would have no reason to expect to have to disclose their votes in the future. In any event, the sign on those institutions is the opposite of the significant sign on the ‘after’ dummy. Hence, the increase in support after the rule appears to be unrelated to institutional votes. In sum, for this category of compensation proposals, there is no apparent impact on voting outcomes from the mutual fund vote disclosure rule.

## **B. Bonus plans**

The results for bonus plan proposals sponsored by management further solidify the view that mutual funds’ voting behavior (and therefore voting outcomes) were not affected by the disclosure rule. Support for these proposals is increasing in mutual fund holdings (see column 2 of Table 5). But none of the interactions with the ‘after’ dummy are significant.

## **C. Proposals to issue or authorize common stock**

The mutual fund vote disclosure rule also has no effect on the voting outcomes of management proposals to authorize or issue common stock., None of the interaction terms between institutional ownership groups and the ‘after’ dummy are significant, as indicated in column 3 of Table 5. Support for these proposals appears to be different from the other management-sponsored proposals: none of the control variables are significant except for bank and insurance company holdings, which are inversely related to voting support, and little variation is explained. We view these results as an indication of the heterogeneity of the proposals in this category (stock is issued for many different purposes), such that voting support is highly proposal-specific.

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opposite.

<sup>38</sup> The rule was adopted under the SEC’s authority to regulate mutual funds and their advisors under the Investment Company Act. The SEC does not have analogous authority over either banks (which are regulated by federal and state banking authorities) or insurance companies (which are regulated by state insurance authorities). None of those regulators indicated at the time of, or subsequent to, adoption of the mutual fund vote disclosure rule that they were

#### D. Shareholder proposals

Table 5 also reports the results for shareholder proposals on takeover defenses and executive compensation (columns 5 and 6, respectively). In contrast to some of the management proposals, there is no effect on the support level for shareholder proposals upon the adoption of the mutual fund vote disclosure rule. The ‘after’ dummy variable, as well as the interaction terms, are insignificant for both proposal categories. Consistent with intuition, support levels for both types of proposals are positively associated with ownership by other institutions, the category that includes the activist investors – public pension and union funds – that sponsor such proposals. In addition, the support level for compensation proposals is marginally inversely related to profitability as measured by ROA. That is also an intuitive result – it is plausible for shareholder dissatisfaction with management, and hence support for proposals to restrict management pay (the aim of the majority of these proposals), to be higher at poorly performing firms.

None of the firms’ takeover defenses are significantly related to support for shareholder proposals on compensation, which is the opposite of the finding concerning management compensation proposals, which obtain lower support in the presence of a poison pill. Takeover defense proposals obtain higher support levels at firms with staggered boards and restrictions on special meetings.<sup>39</sup> Interpretation of the takeover defense variables is, of course, somewhat murkier for these proposals because shareholders will only propose to remove staggered boards or poison pills at firms that have the defenses. If we estimate the regressions for the full sample deleting the staggered board, blank check preferred and poison pill dummies, then none of the findings differ: the coefficients for restrictions on special meetings and other institutions’ holdings are still significantly positive. In addition, if the staggered board (poison pill) proposals are removed and the remaining proposals estimated without the poison pill and blank check preferred (staggered board) dummy variables, again, voting support is still significantly higher for firms with restrictions on special meetings, as well as those with greater holdings by other institutions.<sup>40</sup>

A possible explanation why restrictions on special meetings affect voting outcomes is that when shareholders do not have the option to replace the board at any time by calling a special meeting, they may deem eliminating takeover defenses to be essential for ensuring effective consideration of bids. For example, shareholders

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considering requiring disclosure of their regulated entities’ votes.

<sup>39</sup> The regressors’ VIFs are all low (below 10), indicating that multicollinearity across defenses for the full set of shareholder proposals is not a problem.

<sup>40</sup> There are no proposals to remove restrictions on special meetings or on written consent in the sample. The size of the sample that remains when either the staggered board or poison pill proposals are removed is about the same, 118 or 116 observations (59 or 58 pairs), respectively, both considerably smaller than the full sample of 180 observations (90 pairs). In the regression excluding staggered board proposals (i.e., the regression of votes on proposals to

need not be that concerned over a poison pill or staggered board if at the onset of a hostile takeover they can call a meeting at which they can replace all or part of the board and facilitate the pill's redemption. As a consequence they may be less likely to vote for a proposal to remove those defenses at firms permitting shareholders to call special meetings, as opposed to firms whose corporate charters prevent such action. Although this explanation of the data is speculative, it is consistent with the presence of special meeting restrictions affecting voting outcomes for shareholder proposals on takeover defenses and not for those on executive compensation.

#### **4.3. Inferences from mutual fund votes**

Thus far, we have analyzed the effect of the mutual fund vote disclosure rule on voting outcomes by inference from institutional holdings. As mutual fund votes are available for post-disclosure rule proposals, we can use actual voting data to improve our analysis of whether voting behavior changed. In particular, the previous results only relate the aggregate mutual fund ownership in each firm to voting outcomes. That assumes that all firms are held by funds with similar voting behavior. By using actual voting data and the characteristics of the funds holding our sample firms, we can control for differences in funds across firms. That may be important, as fund holdings are clearly endogenous (especially the holdings of the funds for which we obtain votes, which are funds that have the largest stake relative to their assets under management). Specifically, our previous result that mutual funds did not decrease (and even seemed to have increased) their support for management-sponsored EEIC proposals after adoption of the disclosure rule could be due to changes in which funds hold the firms sponsoring such proposals.

We collect the votes of mutual funds whose holdings of the outstanding shares of the issuer of a sample proposal introduced after the rule change equals at least 0.75 percent of the mutual fund's stock portfolio's assets under management. This criterion results in a sample of funds that are more than average invested in our sample firms, but is not weighted towards larger funds.<sup>41</sup> We identify the funds from Thomson Financial's CDA/Spectrum mutual funds database, which contains quarterly report information on individual mutual funds' domestic equity portfolio holdings.

We seek to predict the mutual funds' actual votes on the 'after' proposals as a function of fund characteristics, which are obtained from the CRSP mutual fund database.<sup>42</sup> The fitted regression of the actual votes

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remove poison pills and all other defenses except for staggered boards), the staggered board dummy is insignificant.

<sup>41</sup> We selected this cutoff for feasibility of data collection. If that cutoff resulted in our collecting votes for less than one-third of the issuer's equity that is held by mutual funds, then for that proposal we used instead a cutoff of 0.25 percent of a fund's stock portfolio.

<sup>42</sup> Because CRSP – Thomson database links are available only for all-equity mutual funds (a subset of the funds in the Thomson database), we obtain fund characteristics for only this subsample of the funds for which we collect votes. This limitation does not affect our results, as the results remain the same if we use for the dependent variable



produces the expected mutual fund vote for all ‘after’ proposals. Applying these coefficients to the fund characteristics at the time of the ‘before’ vote (for which we obviously do not observe actual fund votes), we get an estimate for the expected fund vote variable there as well. Next, we interact the expected fund vote with the percentage of total fund holdings to get an estimate of the total fund vote. This ‘total mutual fund vote’ estimate is then used rather than mutual fund holdings, to refine the previous analysis of whether the mutual fund vote disclosure rule affected fund behavior and consequently, voting outcomes.

Because we only observe the fund vote after the rule change, it is necessary to make an assumption regarding the relation between fund characteristics and voting in order to calculate the expected fund votes before the rule change. We assume that the relationship is stable such that the only change in mutual fund voting (‘before’ versus ‘after’) is related to changes in mutual fund characteristics ‘before’ versus ‘after’, or due to changes in firm characteristics included in our fund vote regression. As a result, in the second-stage regressions that employ the total fund vote estimate, we test a joint assumption: (i) that the fitted fund vote regression contains all of the relevant characteristics (of funds and firms) that affect mutual fund voting, and (ii) that the relation between those characteristics and voting is stable over time. If the coefficient on the total fund vote variable differs ‘before’ versus ‘after’, it could be either because mutual fund votes indeed changed ‘before’ versus ‘after’ in ways that are unrelated to their characteristics, or because of misspecification (i.e., the fitted regression of what factors affect fund voting has omitted important variables that changed ‘before’ versus ‘after’). The assumption of stability functions as a null hypothesis that any change in fund voting after the disclosure rule is not related to fund characteristics.

#### **A. Mutual fund votes and characteristics**

On average, mutual funds voted no differently from other shareholders (73.1 percent in support of proposals compared to 72.7 percent in support overall, see Table 6). However, when votes are disaggregated by proposal type (see Table 6), mutual funds voted against management at a higher frequency than other shareholders for both management-sponsored EEIC proposals and for shareholder-sponsored proposals.<sup>43</sup> Table 6 also shows that mutual fund holding periods are not that long. On average and weighted by fund shares owned, only 38 percent of mutual funds holding stock in the firms at the time of the ‘before’ proposal continued to own shares at the time of

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in the regressions predicting votes only the votes of the funds for which we have characteristics information.

<sup>43</sup> Specific other investors, of course, may have supported management at an even lower level than mutual funds. We sought to compare the funds’ voting to that of CalPERS but were able to identify how CalPERS voted for only eight proposals in our sample. For six of the eight proposals, all of the mutual funds whose votes we obtained voted identically to CalPERS, half of which were positions in support of management. With respect to the other two proposals, in one case all of the funds voted against a shareholder proposal that CalPERS supported (a proposal in the ‘miscellaneous’ category requiring a shareholder vote on executive retirement benefits), and in the other, 70

the ‘after’ proposal, and of those funds for which we collect votes, the average overlapping ownership is an even lower 17 percent. This difference indicates that the holding period for relatively larger stakes is lower than for smaller portfolio holdings.

For the remainder of this section, we focus our analysis on EEIC proposals, the only class of management proposals on which mutual funds voted differently from other investors, and the sample with the most interesting results in the prior section. For comparative purposes we also provide, albeit more briefly, the results for the shareholder-sponsored proposals on takeover defenses, the category of shareholder proposals with the largest sample size and thus offering the most reliable estimation.

Table 7 provides information on the characteristics of the mutual funds holding stock in our sample of firms for these two proposal categories. Average fund characteristics differ significantly over time, with higher average turnover and expense ratios, and lower average net asset values, before the vote disclosure rule was adopted. These differences are consistent with general trends in the mutual fund industry that are independent of the rule change: turnover rates and expenses have declined, and assets have increased, over the past decade.<sup>44</sup> In addition, the table reports the average holdings in the sample firms of the five largest fund families (as measured by their holdings in the sample firms). The average holding varies considerably across the fund families, but is still relatively small, ranging from less than 1 percent to 2 percent. It also varies considerably across sample firms.

The estimated regressions of actual fund votes, which will be used to derive expected fund votes, are reported in Table 8. The fund characteristics used to predict fund votes are expense ratio, turnover ratio, load,<sup>45</sup> the log of total net assets, and the percentage held by the five largest fund families. Because actively managed funds’ voting policies may differ from passively managed funds, we include expense and turnover ratios. We include net assets under management because larger funds have more resources to consider voting issues (firms with fewer resources would, for instance, be more likely to rely primarily on the default rules of proxy voting services, such as ISS). We also include average load, in case funds with sales charges follow different voting policies from funds without sales charges. Given the dramatic alteration in the individual fund characteristics of the average mutual fund over the sample period indicated in Table 7, we de-trend those fund characteristics by subtracting annual means.

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percent of the funds supported a management proposal that CalPERS opposed (an EEIC proposal).

<sup>44</sup> The Investment Company Institute (ICI), the mutual fund trade association, tracks the asset-weighted turnover rate of stock funds, and the ratio ranged between 60 percent and 70 percent through 2001, falling below 60 percent only in 2003 (ICI, 2006: 21). Similarly, average expenses of stock funds have declined from 1.55 percent in 1995 to 1.13 percent in 2005, while assets flowing into no-load funds have continued to increase, and those flowing into load funds have dramatically decreased, from 2000-2005 (ICI, 2006: 18, 39-41). Finally, mutual fund assets have doubled from 1997-2005 (ICI, 2006: 3, 7), the time period of the sample.

<sup>45</sup> The load variable is the sum of the maximum front- and rear-end loads. We average fund characteristics across all funds holding the proposal firms (the regression observation units).

Finally, we include the largest family fund holdings because voting policies are often set at the fund family level, which thereby affects voting outcomes independent of the individual funds' characteristics, and the larger the family holdings the more independently informed the family's voting policies could be. We do not de-trend family fund holdings, however, despite there being a significant increase in most of the families' holdings over time, because holdings could be directly related to voting outcomes if voting policy is set at the family level.

We also include in the regressions firm characteristics that might affect funds' voting policies. The included firm characteristics are the three profitability measures, confidential voting and the five individual takeover defenses used in the regressions reported in the prior sections. As reported in section 4.1, interactions between the 'after dummy' and these characteristics are insignificant, such that the relation between voting outcomes and those characteristics did not change over time.. Consequently, including those variables should improve our ability to predict the 'before' votes with these regressions of 'after' votes.

As Table 8 indicates, the ability of fund characteristics to explain fund votes differs across proposal type, and although most fund characteristic regressors are insignificant, the overall regression is significant (the regression F-statistics are significant at less than 1 percent).<sup>46</sup> The correlation between the expected fund votes (i.e., the fitted values from the regressions in Table 8) and the actual fund votes -- another measure of the goodness of the regression's "fit" -- equals 28 percent for the management-sponsored, and 60 percent for the shareholder-sponsored, proposals, both of which are highly significant. This lends confidence to the efficacy of using the two-stage approach. As the next two sections report, in general, the results of the voting regressions using expected votes replicate those reported earlier for the regressions inferring mutual fund voting from mutual fund holdings that are estimated without the additional information that can be gleaned from some funds' actual votes.

## **B. Total mutual fund votes and EEIC proposals**

The first 3 columns in Table 9 report the results for EEIC proposal voting outcomes using our estimate of the 'total mutual fund vote,' which is computed by multiplying the total mutual fund ownership by the expected

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<sup>46</sup> Regressions in Table 8 are estimated using all funds and not solely those for which we collect votes, on the assumption that the funds for which we have votes are representative of all of the funds holding the shares. There are too many cases of "zero" observations for family fund holdings to be able to estimate the regressions reliably for those variables using only the smaller number of funds for which we collect votes (for example, there are 350 zero observations for the Fidelity fund family). Regressions using only funds for which we collect votes can be estimated if the fund family holding variables are excluded. Compared to a regression using all observations on only the individual fund and firm characteristics in the reported regressions, the regressors using only funds for which we have votes are less significant. Also, if the fund characteristic variables are not adjusted by their annual means, their significance levels are unchanged but the significance of some of the fund family holdings variables decreases.

mutual fund vote fitted from column 1 of Table 8.<sup>47</sup> We also include the new variable ‘percent same,’ which is the percentage of continued share ownership by mutual funds across the ‘before’ and ‘after’ proposals for which we obtain the funds’ votes. If this percentage is relatively high, the funds holding that stock before the rule change should be relatively more similar to the funds holding that stock after it. Firms for which this percentage is relatively low should be more likely to have funds whose characteristics differ before and after the rule change (because there is a greater difference between which funds own the stock before and after). As we find that ‘percent same’ is never significant, this suggests that differences in funds holding the firm (and thus their characteristics) ‘before’ versus ‘after’ are not significantly related to aggregate voting outcomes. This lends support to the assumption underlying the regression predicting fund votes that the relation between fund characteristics and fund votes is stable over the period before and after the rule change.

Columns 1 and 2 of Table 9 indicate that the added information from fund votes and characteristics increases the statistical power of the analysis and confirms the previous results: the coefficient of the total fund vote unconditionally is negative and interacted with the ‘after’ dummy positive, and both are clearly statistically significant. These columns closely parallel the specifications in column 1 of panel A of Table 4, where no fund-specific information is used, and the corresponding coefficients using fund holdings are only marginally significant.

The regression in column 1 of Table 9 can be used to estimate economically how mutual fund voting could impact the overall voting outcome. For example, we can consider the impact of an increase of the expected vote by mutual funds by a one standard deviation shock (equal to 0.07 either before or after the rule change). The net effect after is zero, but the net effect before lowers the logit-transformed vote (by  $-1.6 \times 0.07 = 0.11$ ) and thus the actual vote by approximately 2.0 percent.<sup>48</sup>

The result – that fund voting support increased after the rule change - continues to hold when all of the firm characteristics are included (see column 2) that were also used in the fund vote regressions (see Table 8). Finally, the regression model in column 3 of Table 9 parallels the specification in column 3 in panel A of Table 4 using board governance variables, and those previous results are essentially replicated.

Therefore, while the raw data reveal that mutual funds are less likely to vote for management than all other investors, their lower level of support is not a function of the vote disclosure rule. For that to be the case, the ‘after’-

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<sup>47</sup> Because mutual fund holdings data were not available for each sample firm for both before- and after- disclosure rule change proposal years, the sample for the analysis using actual votes is smaller than that for the prior analysis: 362 ‘after’ proposals are used in the derivation of expected votes. The second-step estimates take the estimation risk of the first-step into account by bootstrapping the first-stage residuals and adding those residual estimates to the fitted values of the expected fund vote. We report the mean coefficients and their mean robust standard deviations, obtained by averaging over 10,000 bootstraps.

<sup>48</sup> This is only an approximation of the effect because of the non-linear transformation of the dependent variable; we

interaction must be significantly negative as well. However, these new results indicate more strongly than the analysis in Table 4 (that did not use information from the actual fund votes) that the disclosure rule increased, rather than reduced, mutual funds' voting support for management on EEIC proposals. The 'after' interaction is significantly positive. Accordingly, this main result seems robust to controlling for the endogeneity of which types of funds hold firms with EEIC proposals. An alternative interpretation of the result could be that the relation between fund characteristics and fund votes is not stable over time, such that funds with the same characteristics voted in support of management after, and against management before, the rule change. Although we prefer the former explanation because the 'percent same' variable is insignificant, neither interpretation is consistent with the rationale for the vote disclosure rule of its advocates, that transparency would lower mutual funds' support for management.

### **C. Total mutual fund votes and shareholder-sponsored proposals on takeover defenses**

Regressions using the total fund vote estimate to explain voting outcomes for shareholder proposals to remove takeover defenses are reported in columns 4 and 5 of Table 9.<sup>49</sup> These results parallel those previously reported (see column 4 of Table 5). Confirming intuition, voting support for the proposals increases with the holdings of other institutions, the institutional investor category including public pension funds and other activist shareholders. In addition, restrictions on shareholders' right to call special meetings increase voting support.

In the regression reported in column 4 that omits firm characteristics included in the regression on actual mutual fund votes, the total fund vote variable is significantly positive, although the total fund vote interacted with the 'after' dummy is insignificant. However, when all firm characteristics are included in the regression (column 5), neither are significant, nor are any of the interactions of the other institutional holdings groups with the 'after' dummy significant. Thus, we continue to find that mutual funds' voting behavior on shareholder proposals was not affected by the vote disclosure rule.

### **5. Selection of before-and-after EEIC proposals pairs and endogeneity**

A possible explanation for our main result that mutual funds seem to have increased their support for management-sponsored EEIC proposals is our selection procedure of the similar 'before' and 'after' proposal pairs for the same firm. The endogeneity issue is that having a proposal both before and after the rule change is a choice

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compute the impact at the average voting outcome.

<sup>49</sup> In contrast to the regression for the EEIC proposals, due to the much smaller sample of shareholder proposals in which more than half of the actual votes outcomes equal 100 percent, i.e., all mutual funds voted for the proposal,

by management. For example, management may be more likely to sponsor a proposal in any given year if they expect the proposal to pass. Further, this may be related to our main variable of interest, mutual fund holdings.

To investigate this for the EEIC proposals (our largest group of proposals and those with our strongest results), we create a matched sample of firms that had only a ‘before’, but no ‘after’, EEIC proposal. We first describe our matching procedure and any differences between our sample of original firms (those with both ‘before’ and ‘after’ proposals) and our sample of matches (those with only ‘before’ proposals). Second, we will attempt to see if differences in firm characteristics, both before or after the rule change, are associated with having no proposal afterwards and discuss the extent to which that may partly explain our results.

### **5.1 Match sample: construction and comparison of matched firms to the original sample**

We start with the universe of firms in the IRRC proxy voting database from 1994-2005 to identify matches for our sample firms, namely firms with an EEIC proposal offered prior to the disclosure rule and no such proposal after the rule change.<sup>50</sup> From that pool of firms, we select a match for each sample firm by IRRC proposal code (and year if possible), by size (market capitalization) and by two-digit SIC code, measured in the year of the ‘before’ proposal.<sup>51</sup> We end up with a total of 254 usable matches (match firms with no missing information on the basic controls or institutional holdings).<sup>52</sup>

Table 10 presents the difference between the original firms and the match firms, for

- (i) ‘before’ proposals, using the actual proposal dates for both original and match firms.
- (ii) ‘before’ proposals, using the dates for the original firms for both the original and the match firms.

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fifteen expected fund votes exceeded 100 percent. Those estimates were replaced with 100 percent in our analysis.

<sup>50</sup> In constructing the sample we found that the IRRC voting data were incomplete in the post-rule period (some firms followed before 2003 were not followed thereafter or their 2004 votes were not collected and the firms’ post-rule EEIC proposals did not show up in the database). We therefore reviewed all post-rule proxy statements of each potential match for EEIC proposals submitted after the rule change to make sure that the matches were clean. Matches can have proposals offered after the rule change, as long as those proposals do not fall into any of the IRRC issue codes for EEIC proposals.

<sup>51</sup> Given the three-pronged matching process, for 35 matches the difference in size is large (100 percent). Fifteen sample firms are matched on one-digit SIC codes because there were no two-digit SIC code matches at all or none within 100 percent of the sample firm’s size. When matching on IRRC proposal, if there is no firm with a same code proposal in the same year as the original firm’s proposal (and whose size is within 100 percent of the original firm’s size), we select the proposal offered in the closest year to the year of the original firm’s proposal, choosing a year after over a year before the original firm’s proposal year, if there is a tie in distance.

<sup>52</sup> Because that procedure results in some sample firms being assigned to the same match firm, we identify alternative matches, using the same criteria (but typically selecting a firm less close in size), so that we have unique matches where necessary for analysis. If a match firm is assigned to two sample firms for which both the ‘before’ and ‘after’ years differ, then because the match observations will be taken from different years, that match is considered to be unique. For a benchmark analysis, we compare the matches to the original firms using the year in which the match firm’s proposal was offered. In that analysis, multiply-used matches considered unique because sample firms’ proposal years differed are no longer unique and are excluded (i.e., only one pair with the match firm is included). For that analysis there are only 200 usable matches, but results are similar.

(iii) ‘after’ proposal dates, which of course are only available for the original firms.

On most firm-level dimensions, the groups of firms are very similar, even though the matching criteria were based on industry and firm size only. For some variables, it matters which dates are considered for the matched firms (own proposal or original sample firm’s ‘before’ proposal year). Those differences can generally be explained by noting that the proposal dates for the original firms before the rule change are generally earlier than those for the match firms.<sup>53</sup> The main differences for the two groups are that the match firms without an ‘after’ proposal seemed to have smaller size and lower institutional holdings, along with greater support for their EEIC proposals (by 2 percent).<sup>54</sup> But most importantly, there is no discernable difference in mutual fund holdings across the two groups in the ‘before’ period.

Table 10 next reports the differences for these firm variables for the dates of the proposals of the original firms after the rule change, and the difference-in-difference of how each variable changed from the original firms’ ‘before’ proposal date.<sup>55</sup> For four variables, there is a significant difference for the original firms versus the match firms: firms without ‘after’ proposals experienced lower growth in market capitalization, a reduction in market beta, an increase in the holdings of independent investment advisors and a decrease in the holdings of mutual funds. Clearly, those variables that differ across groups (and especially those that changed differently after the vote disclosure rule change across groups) are the prime variables of interest in our consideration of whether endogeneity could explain our main result, that funds’ support for management increased rather than decreased after the rule change.

## 5.2 Exploring endogeneity

As a benchmark for whether our matching procedure will assist in identifying endogeneity in proposals offered after the rule change, we first examine whether there are differences in explanatory factors for the voting outcomes of the match firms’ proposals and the original sample firms’ ‘before’ proposals. To investigate how the voting outcomes for all those proposals before the rule change differ for our original sample firms versus the match firms, we use an ‘original’ dummy to indicate an original sample firm and interact the independent variables with this ‘original’ dummy. The results are reported in Table 11.

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<sup>53</sup> The before proposals of the original firms are on average 3 months earlier than the match firms.

<sup>54</sup> When measured at the time of the actual match firms’ ‘before’ proposal, size is no longer significant and different non-mutual fund institutional holdings are significant (see Table 10).

<sup>55</sup> The difference-in-difference in column 4 in Table 10 is not equal to the difference of the values in columns 2 and 3 of the table, because for columns 2 and 3, the requirement for a pair’s inclusion is no missing information for either the ‘before’ or the ‘after’ dates, but for column 4 the requirement is no missing data for both dates. As a result,

The ‘original’ dummy itself is always insignificant. In addition, the interactions of the institutional holdings with the ‘original’ dummy are all insignificant (see column 2 of Table 11). If all independent variables are added with the ‘original’ dummy interaction in column 3, none of the coefficients are clearly statistically significant. Two coefficients are marginally significant, namely turnover and holdings of other institutions, which includes pension and hedge funds. These results indicate that the effect on voting outcomes of firm characteristics is essentially indistinguishable across the two groups of firms. This provides support for using the matching process to examine endogeneity in post-rule proposals (since as best as we can tell, the factors affecting the baseline voting before the rule change in the two sets of firms are the same).

Table 12 presents the results for logit regressions estimating the likelihood of not having an EEIC proposal after the rule change (i.e., the dependent variable equals 1 for match firms). Our sample consists of those original-firm – match-firm pairs for which we have no missing information. We include the basic controls plus the institutional holdings. For all these variables, we include both the value before the rule change (at the date of the proposal of the original firm, for the relevant match firm as well), and the change in that value from the original firms’ ‘before’ proposal date to the date of its proposal after the rule change. We further include the voting outcome of the ‘before’ proposal as an independent variable. If management is more likely to put up proposals that it thinks will pass, then more shareholder support on the previous vote may be associated with a higher likelihood of another proposal being put up, suggesting a negative coefficient. Finally, we include the number of months since the ‘before’ vote (i.e., the difference between the date of the original firm’s ‘after’ proposal and the date of the firms’ actual proposals in the ‘before’ period), in case a longer period would make it more likely for a firm to revisit its previous plan, independent of other firm characteristics, which would again suggest a negative coefficient. Results are reported for two logit estimations, one including and the other excluding the two accounting profitability measures.

The results indicate that across the two logit specifications, the main variable that is consistently and statistically significantly related to the likelihood of having no proposal after the rule change is the holdings by mutual funds. Specifically, both larger mutual fund holdings ‘before’ and a large increase in mutual fund holdings ‘after’ are associated with a greater chance of having a proposal after the rule change (the former is marginally significant with a p-value of 8 percent and the latter is clearly significant with a p-value of less than 3 percent). In addition, in the full model of column 2, three other variables’ ‘before’ levels are positively related to the likelihood of having an ‘after’ proposal: holdings by banks and insurance companies, restrictions on shareholders’ ability to

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the samples are different.



call special meetings, and NPM (the latter two being only marginally significant at 10 percent). However, for none of those three variables are changes from ‘before’ to ‘after’ significant. Interestingly, neither the ‘before vote outcome’ nor the ‘time since the before vote’ variables are consistently significant (the former being insignificant and the latter being significant only in column 1, though with a positive coefficient, the opposite of the expected sign). This suggests that the a priori endogeneity concerns are not that important.

Table 12 provides some evidence that, after the rule change, management seems more likely to sponsor EEIC proposals in relation to ownership composition. As we previously found that after the rule change mutual funds show greater support for these proposals, the increased likelihood of having a proposal after the rule change for firms with a greater increase in mutual fund holdings could explain part of our results.

However, this result would not be predicted by the overall association between mutual fund voting before the rule change, which (see panel A of Table 4 and Table 9) indicated that, if anything, higher voting outcomes were associated with lower mutual fund holdings. Moreover, as previously reported, if we regress the voting outcome of the ‘before’ proposals of both original firms and match firms jointly on their firm characteristics, we do not find any difference between the support of these proposals and the level of mutual fund holdings across the two groups.

It is possible that management correctly anticipated the increased support of mutual funds after the rule change, but any such increase would have been against the anticipation of the advocates for the disclosure rule. On the other side, as Table 6 indicates, mutual fund support for EEIC proposals is still lower than that of the average shareholder. A related explanation could be that management was able to anticipate correctly which proposals would find increased support by mutual funds. For example, Table 8 suggests that for the ‘after’ proposals, mutual funds are more likely to support the proposal if the firm has a higher NPM (marginally significantly positive). Firms with a higher NPM at the time of the ‘before’ proposal were also marginally significantly more likely to have an ‘after’ proposal in our sample.

## **6. Conclusion**

This paper investigates whether the SEC’s requirement of mutual fund proxy vote disclosure impacted the voting behavior of the funds and voting outcomes for a broad set of management- and shareholder- sponsored proxy proposals by comparing outcomes of similar proposals sponsored at the same firm both before and after the rule change. We do not find any evidence that the rule altered mutual funds’ behavior as predicted by the rule’s advocates and as perhaps feared by its opponents: support for management did not decline after the rule’s implementation. Rather, we find some evidence that mutual funds’ support for management has increased after the

disclosure of their votes, for management-sponsored proposals on executive equity incentive compensation plans (EEICs). In addition, having greater ownership by mutual funds is associated with a higher likelihood of management sponsoring such a proposal after the rule change. For the subset of sample firms for which we have board ownership data, we further find that the funds' increased support for such proposals after the rule change is related to the magnitude of independent directors' shareholdings. For the other management and shareholder proposals in the sample, there is no evidence of any change by mutual funds post-vote disclosure.

Overall support for management has declined from a decade ago, when the bulk of prior research on shareholder proxy proposals was undertaken. The average support level for the shareholder proposals in our sample is much higher than that reported in the earlier literature, and that for management-sponsored proposals is lower, particularly for EEIC proposals. Institutional ownership has increased at the same time as support for management has been decreasing. We do not offer an explanation of the decline in support. However, we can reject several alternatives. Besides rejecting the mutual fund vote disclosure rule as the cause of the decline in management support, we also do not find evidence that the decline is explained by the impact of SOX. That is because the negative association between later sample years and voting outcomes is greater post-June 2003 (the effective implementation of the voting disclosure rule) than post-July 2002 (SOX's enactment). In addition, the finding regarding EEIC proposals is not a function of changes in compensation plan characteristics or the elimination of broker votes as of July 1, 2003.

Finally, we find that takeover defenses do not have a uniform effect on voting outcomes. Some defenses reduce support for management in some voting contexts: poison pills lower support for management-sponsored EEIC proposals, and restrictions on special meetings increase support for shareholder-sponsored proposals to remove takeover defenses. However, other defenses are associated with higher support for management. Moreover, as they depend on the model specification, these results are not consistent within, just as they are not consistent across proposal types. These data suggest that investors may have a more nuanced view of the significance of takeover defenses when considering whether to support particular management initiatives, than that taken in the academic literature that conventionally characterizes defenses as entrenching and always against shareholders' interests.

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**Table 1. Sample Construction**

The table presents the number of firms in the sample and the number of proposal pairs, which means proposals with the same IRRC codes both before and after the mutual fund vote disclosure rule's effective date (July 1, 2003). Because some firms that have more than one matched proposal pair have either dual class stock, missing voting data, or missing accounting performance data, for some but not all proposals, the number of firms is not a sum.

<b>Sample</b>	<b>Number of Proposal Pairs</b>	<b>Number of Firms</b>
Total matched pairs	1,006	680
Pairs at firms with dual class stock	112	73
Pairs with proposal(s) missing voting outcomes	26	21
Pairs missing other data	15	13
Sample matched pairs	853	582

**Table 2. Types of Proposals and Voting Outcomes in Relation to the Mutual Fund Vote Disclosure Rule**

The table presents voting outcomes (average percentages voting for and voting against) for our sample's proposals by type (management or shareholder-sponsored) and within type by group, detailing the IRRC codes comprising the groups, over the full time period as well as split at the rule's effective date, July 1, 2003 ('votes for before' and 'votes for after'), and the t-statistic for the difference in mean between the percentages of votes for before and votes for after calculated pairwise; \*\* means significant at less than 5 percent and \* means significant at 10 percent; N/A means statistical test non-applicable.

<b>Proposal Type</b>	<b># of proposal pairs</b>	<b>IRRC codes*</b>	<b>Votes for</b>	<b>Votes against</b>	<b>Votes for before</b>	<b>Votes for after</b>	<b>T-stat difference in mean</b>
<i>All Management</i>	673	1100-1589	81.7	15.9	82.9	80.5	4.67**
Common stock issuance	68	1100-03	80.1	9.9	79.5	80.6	-0.67
Miscellaneous	10	1020, 1151, 1332	92.8	2.7	94.4	91.3	0.98
Remove defenses	3	1402, 1444	72.5	4.7	66.5	67.3	-1.39
Merger	1	1200	69	0.6	70.4	78.4	N/A
<i>All Compensation</i>	591	1500-1589	81.8	16.8	83.2	80.4	5.39**
Executive equity incentive plan (EEIC)	408	1500-09; 1530-39	77.6	20.9	78.9	76.2	3.91**
Outside director equity incentive plan	36	1510-19; 1540-49	83.5	15.3	86.3	80.7	3.12**
Employee stock purchase plan	77	1520-29	92.9	6.3	94.3	91.4	2.72**
Bonus plan	70	1560-64, 1580-82	93.2	5.7	93.9	92.4	1.73*
<i>All Shareholder</i>	180	2000-2906	42.8	56.9	40.1	45.5	-4.77**
Takeover defenses	90	2220, 2300-41	57.4	42.2	54.9	59.9	-3.7**
Executive compensation	57	2400-14	32.7	67.1	28.6	36.9	-3.83**
Board independence	18	2201-14	22.8	77	23.4	22.3	0.4
Director elections	1	2231	9	91	8.2	9.7	N/A
Miscellaneous	14	2002, 2030, 2131, 2342, 2417, 2901, 2906	18	81.8	15.6	20.5	-0.75

### **Table 3. Descriptive Statistics - Mean and Standard Deviation**

The table presents descriptive statistics of firm-level characteristics at firms that had a proposal pair before and after the mutual fund vote disclosure rule's effective date of July 1, 2003. For all characteristics, we report the mean, with the standard deviation given between parentheses, calculated for all proposals, for manager- versus shareholder-sponsored proposals, and for proposals offered 'before' versus 'after' the rule change. 'Return(-12)', 'Turnover (-12)' and 'Market return (-12)' are the average monthly return, the average monthly turnover (in percentages) and the average monthly value-weighted market return, respectively, in the 12 months before the proposal's meeting date. 'Beta(-60)' is the firm's market beta estimated using the 60 monthly returns before the proposal's meeting date. These variables are obtained from the University of Chicago Graduate School of Business Center for Research in Securities Prices (CRSP) database. 'ROA' is the return on assets and 'NPM' is the net profit margin from the annual Compustat file for the previous fiscal year. 'Institution pct' is the percentage of equity held by institutional investors. 'Banks,' 'Insurance cos,' 'Mutual funds', 'Ind investment advisors' and 'others' are the percentage held by those types of institutional investors, where 'Mutual funds' includes mutual funds and mutual fund investment advisors and 'Other institutions' includes university endowments, private and public pension and labor union funds. All institutional holdings are for the quarter before the proposal's meeting date and are obtained from Thomson Financial Services. 'Classified board' is a dummy variable for the presence of a staggered board; 'Special meeting restr.' is a dummy variable for restrictions on shareholders' ability to call special meetings; 'Written consent restr.' is a dummy variable for restrictions on shareholder action by non-unanimous written consent; 'Poison pill' is a dummy variable for the presence of a poison pill; 'Blank check preferred' is a dummy variable for the ability to issue blank check preferred stock, and 'Confidential voting' is a dummy variable for confidential voting of proxies. These variables are obtained from IRRC's governance database or hand-collected from the firms' SEC filings. 'Pct bd independent' is the percentage of independent directors on the board; 'Number directors' is the number of directors, abbreviated as 'Numdir' in interaction terms in subsequent tables; 'Ind directors stock' and 'Inside directors stock' are the percentages of equity held by independent (non-employee and non-affiliated) and insider directors, respectively, and in subsequent tables are abbreviated as 'Indstk' and 'Insidestk' in interaction terms. These variables are obtained from the IRRC's directors database. 'Dilution prop' is the dilution caused to a firm's outstanding shares by a specific proposal on an executive equity incentive compensation plan (EEIC); 'Total dilution' is the dilution due to all compensation plans outstanding at the time a proposal is presented and not just that due to the specific proposal being voted on; 'Repricing' is a dummy variable indicating that the proposed plan permits repricing of underwater options; 'Loans' is a dummy variable indicating that the proposed plan permits the extension of credit to executives to purchase stock or exercise options granted by the plan; 'restricted stock' is a dummy variable indicating that the plan permits awards of restricted stock; and 'Dilut less than 5%' is a dummy variable indicating that the dilution caused by the proposed plan (its 'dilution proportion') is less than 5 percent. These variables are obtained from the IRRC. 'Difference in prop. year' is the difference between the 'before' and the 'after' proposal year. The mean values are computed only for firms for which data are available at the time of both the 'before' and 'after' proposals, as those are the observations that are used in the regressions reported in the subsequent tables; + indicates that the variable was obtained only for management-sponsored EEIC proposals.

<b>Variable</b>	<b>Full sample</b>	<b>Management proposals</b>	<b>Shareholder proposals</b>	<b>Before proposals</b>	<b>After proposals</b>
Market cap (000s)	14738866 (38442687)	8647607 (21650885)	37513407 (67847286)	13336481 (37816888)	16141251 (39030244)
Return (-12)	0.0173 (.03)	0.0201 (.04)	0.007 (.03)	0.0089 (.04)	0.0257 (.03)
Turnover (-12)	1.7 (1.5)	1.8 (1.6)	1.3 (.86)	1.7 (1.6)	1.8 (1.3)
Beta (-60)	0.1534 (.11)	0.1516 (.10)	0.1599 (.13)	0.16 (.11)	0.1472 (.10)
Market return (-12)	0.008 (.02)	0.0088 (.01)	0.0052 (.02)	-0.0004 (.02)	0.0164 (.01)
ROA	0.0377 (.11)	0.0413 (.11)	0.0245 (.10)	0.0404 (.10)	0.0351 (.12)
NPM	0.0525 (.16)	0.0515 (.17)	0.0561 (.11)	0.0495 (.16)	0.0555 (.16)
Institution pct	0.7054 (.18)	0.7115 (.18)	0.6826 (.15)	0.6632 (.18)	0.7476 (.16)
Banks	.1109 (.05)	0.1039 (.05)	0.1368 (.07)	0.107 (.06)	0.1148 (.05)
Insurance cos	0.0484 (.03)	0.0481 (.03)	0.0497 (.03)	0.0501 (.04)	0.0467 (.03)
Mutual funds	0.1785 (.09)	0.179 (.09)	0.1765 (.08)	0.1752 (.09)	0.1818 (.09)
Ind investment advisors	0.2305 (.09)	0.2409 (.10)	0.1914 (.08)	0.2259 (.10)	0.235 (.09)
Other institutions	0.1372 (.07)	0.1396 (.08)	0.1282 (.05)	0.1050 (.06)	0.1694 (.07)
Classified board	0.6231 (.49)	0.6152 (.49)	0.6528 (.48)	0.6295 (.48)	0.6166 (.49)
Special meeting restr.	0.5258 (.5)	0.4978 (.50)	0.6306 (.48)	0.4959 (.50)	0.5557 (.50)
Written consent restr.	0.493 (.5)	0.4695 (.50)	0.5806 (.49)	0.4783 (.50)	0.5076 (.50)
Poison pill	0.5733 (.5)	0.5958 (.49)	0.4889 (.50)	0.558 (.50)	0.5885 (.49)
Blankcheck preferred	0.9127 (.28)	0.9131 (.28)	0.9111 (.29)	0.9062 (.29)	0.9191 (.27)
Confidential voting	0.1794 (.38)	0.1226 (.33)	0.3917 (.49)	0.163 (.37)	0.1958 (.40)
Ind directors stock	0.0044 (.02)	0.0046 (.02)	0 (0)	0.0046 (.02)	0.0041 (.02)
Inside directors stock	0.0502 (.11)	0.0523 (.11)	0.0026 (.01)	0.0528 (.11)	.0476 (.11)
Number directors	10 (2.7)	9.9 (2.7)	12.5 (2.7)	10.1 (2.9)	10 (2.6)
Pct bd independent	0.6815 (.18)	0.6773 (.18)	0.7753 (.12)	0.6647 (.19)	0.6983 (.16)
Dilution prop +		4.7 (2.9)		4.74 (2.7)	4.67 (3.2)
Total dilution +		19.3 (13.7)		18.4 (8.0)	20.1 (17.6)
Repricing +		.21 (.41)		.35 (.48)	.07 (.26)
Loans +		.25 (.44)		.42 (.5)	.34 (.47)
Restricted stock +		.83 (.38)		.55 (.5)	.69 (.46)
Dilut less than 5% +		.65 (.48)		.67 (.47)	.62 (.49)
Difference in prop. year	3.41 (2.04)	1.74 (1.40)	3.85 (1.96)		

**Table 4, Votes ‘Before’ and ‘After’ for EEIC Proposals**

The table reports the pooled panel regression results for all EEIC proposal pairs, with one proposal before and one after the mutual fund vote disclosure rule’s effective date (July 1, 2003). For a description of the variables, see Table 3; ‘\*after’ is an interaction with an ‘after’ dummy variable indicating the proposal was adopted as of the rule’s effective date; ‘\*after\_SOX’ is an interaction with an indicator variable for a proposal after the enactment of the Sarbanes-Oxley Act (post-July 2002); Robust standard deviations are given between parentheses.

**Panel A. Votes ‘Before’ and ‘After’: Main Results**

<b>Variable</b>	<b>(1)</b>	<b>(2)</b>	<b>(3)</b>	<b>(4)</b>	<b>(5)</b>
Constant	1.6 (.4)**	.57 (.84)	.54 (.81)	1.9 (.41)**	1.7 (.42)**
After	-.27 (.24)	-.63 (.55)			-.10 (.41)
Ln (Market cap)	.05 (.03)*	.13 (.06)**	.12 (.06)**	.04 (.03)	.05 (.03)*
Return (-12)	-.68 (.86)	-3.4 (1.7)**	-3.3 (1.7)**	-.62 (.87)	-.48 (.86)
Beta(-60)	.22 (.3)	.08 (.58)	.03 (.58)	.20 (.3)	.17 (.3)
Market return (-12)	1.8 (2.4)	-.38 (4.9)	2.5 (4.7)	-.63 (2.0)	2.2 (2.5)
Turnover(-12)	-.14 (.02)**	-.14 (.05)**	-.15 (.05)**	-.14 (.03)**	-.15 (.02)**
ROA	-.85 (.46)*	-1.3 (1.0)	-1.4 (.99)	-.79 (.47)*	-.83 (.47)*
NPM	.66 (.35)*	1.7 (.64)**	1.8 (.63)**	.62 (.35)*	.66 (.34)*
Confidential voting	-.14 (.09)	-.34 (.16)**	-.30 (.16)*	-.13 (.09)	-.14 (.09)
Blank check preferred	-.13 (.1)	.02 (.17)	.07 (.17)	-.13 (.10)	-.13 (.1)
Classified board	.11 (.06)*	.25 (.11)**	.24 (.12)**	.10 (.06)	.11 (.06)*
Special meeting restr.	-.03 (.06)	-.2 (.11)*	-.23 (.11)**	-.04 (.06)	-.03 (.06)
Written consent restr.	.009 (.06)	-.08 (.11)	-.06 (.11)	-.002 (.06)	0.002 (.06)
Poison pill	-.20 (.06)**	-.13 (.12)	-.14 (.11)	-.20 (.06)**	-.19 (.06)**
Banks & insurance cos	-.07 (.66)	-.11 (1.3)	.38 (1.1)	.14 (.74)	-.20 (.73)
Mutual funds	-.84 (.44)*	-.45 (.70)	-.45 (.70)	-.54 (.52)	-.50 (.52)
Ind investment advisors	-.36 (.43)	-.40 (.88)	-.27 (.81)	-.75 (.49)	-.77 (.5)
Other institutions	-.93 (.76)	-1.2 (1.3)	.30 (1.1)	-2.2 (.86)**	-1.8 (.88)**
Banks& insurance*after	-.11 (.92)	.95 (2.1)	-.15 (1.4)		-.09 (1.6)
Mutual funds*after	1.1 (.6)*	1.4 (2.9)	1.0 (.86)		1.9 (.89)**
Ind invt advisors*after	-.27 (.56)	-.08 (1.2)	-1.0 (.93)		-.94 (.84)
Other*after	.16 (.95)	1.6 (1.7)			-1.5 (1.9)
Ind directors stock		.63 (2.9)	1.2 (3.1)		
Inside directors stock		.55 (.80)	.003 (.49)		
Number directors		-.03 (.02)	-.04 (.02)*		
Pct bd independent		-.45 (.43)	-.39 (.32)		
Indstk*Mutfund*after		59.1 (24)**	117 (39)**		
Insidestk*Mutfund*after		-11.6 (8.1)			
Pct bd ind*Mutfund* after		1.7 (3.6)			
Numdir*Mutfund*after		-.1 (.19)			
Indstk*Banks&insur*after			22 (43)		
Indstk*InvtAdv*after			53 (25)**		
Indstk*Other*after			-128 (38)**		
After_SOX				-.36 (.25)	-.30 (.41)
Banks& insurance*after_SOX				.09 (.94)	-.11 (1.6)
Mutual funds*after_SOX				.49 (.63)	-1.1 (.93)
Ind invt advisors*after_SOX				.38 (.60)	1.1 (.91)
Other*after_SOX				1.3 (1.0)	2.6 (2.0)
R2	.1667	.2468	.2423	.1640	.1743
# of observations	816	258	258	816	816



**Table 4, Panel B. Regressions with Compensation Plan Features**

Variable	(1)	(2)	(3)	(4)
Banks & insurance cos	-2.3 (.90)**	-1.9 (.88)**	-1.8 (.82)**	-1.9 (.85)**
Mutual funds	-.77 (.76)	-.78 (.70)	-.71 (.63)	-.95 (.66)
Ind investment advisors	-.19 (.61)	-.20 (.57)	-.21 (.54)	-.22 (.54)
Other institutions	-.5 (1.1)	-.74 (.70)	-.70 (.65)	-.68 (.69)
Banks& insurance*after	.07 (1.3)	-.68 (.96)	-.94 (.85)	-.74 (.92)
Mutual funds*after	.04 (.86)	.12 (.75)		.15 (.73)
Ind invt advisors*after	-.57 (.79)	-.59 (.65)	-.69 (.61)	-.68 (.62)
Other*after	.01 (.01)			
Total dilution	-.02 (.01)**		-.02 (.01)*	-.02 (.01)**
Dilution proportion	-.06 (.02)**	-.07 (.02)**	-.06 (.02)**	
Restricted stock	-.12 (.10)			
Repricing	-.37 (.12)**	-.47 (.12)**	-.44 (.12)**	-.42 (.11)**
Loans	-.15 (.09)			
Totaldilution*after		-.01 (.005)**		
Dilutionprop*after		.01 (.02)		
Repricing*after		.31 (.25)		
Mutfund*totaldilution*after			-.01 (.03)	
Mutfund*dilutionprop*after			-.002 (.11)	
Mutfund*repricing*after			.94 (1.3)	
Dilution less than 5%				.28 (.12)**
Dilution less than 5%*after				-.10 (.15)
Controls of panel A included	Yes	Yes	Yes	Yes
R2	.3646	.3215	.3532	.3286
# of observations	310	342	342	342

**Table 5, Votes ‘Before’ and ‘After’: Other Proposals**

The table reports the pooled panel regression results for all management-sponsored proposals (MP) on employee stock purchase plans (column 1), bonus compensation plans (column 2) and on the issuance or authorization of common stock (column 3), and for all shareholder-sponsored proposals (SP) on takeover defenses (column 4) and executive compensation (column 5), for all firms with proposal pairs, thus one proposal before and one after the mutual fund vote disclosure rule’s effective date (July 1, 2003). For a description of the variables, see Table 3; “\*after” indicates an interaction between the variable and an ‘after’ dummy variable indicating the proposal was adopted as of the rule’s effective date. Robust standard deviations are given between parentheses, \*\* means significant at less than 5 percent and \* means significant at 10 percent.

<b>Variable</b>	<b>MP: Employee Stock Purchase Plans</b>	<b>MP: Employee Bonus Plans</b>	<b>MP: Common Stock Issues</b>	<b>SP: Takeover Defenses</b>	<b>SP: Executive Compensation</b>
Constant	1.5 (1.1)	1.9 (.89)**	2.0 (1.0)*	.43 (.76)	-2.7 (2.5)
After	1.9 (.93)**	-.23 (.46)	-.76 (.68)	.15 (.54)	1.2 (.9)
Ln (Market cap)	.05 (.06)	.02 (.05)	.01 (.07)	-.11 (.05)**	-.05 (.13)
Return (-12)	.17 (1.9)	1.1 (1.8)	4.4 (3.0)	-.36 (2.1)	.60 (3.2)
Beta(-60)	-1.3 (1.3)	-.11 (.55)	.85 (.73)	-1.0 (.39)**	-.02 (.9)
Market return (-12)	4.9 (9.6)	6.3 (4.9)	-4.3 (8.8)	4.1 (6.4)	2.3 (9.8)
Turnover(-12)	-.04 (.04)	.02 (.05)	.04 (.09)	-.17 (.09)*	.22 (.10)**
ROA	.89 (1.1)	1.2 (1.1)	-1.0 (1.2)	.10 (.81)	-3.8 (2.1)*
NPM	-.58 (.60)	-1.2 (1.0)	.48 (.66)	.82 (.89)	.53 (1.6)
Confidential voting	-.67 (.32)**	-.19 (.14)	.07 (.21)	.21 (.11)*	.05 (.29)
Blank check preferred	-.25 (.23)	.54 (.38)	-.15 (.32)	-.33 (.25)	-.20 (.48)
Classified board	.16 (.18)	.01 (.11)	.17 (.16)	.40 (.12)**	.42 (.31)
Special meeting restr.	-.02 (.22)	.2 (.13)	.25 (.15)	.43 (.12)**	.33 (.26)
Written consent restr.	-.05 (.16)	-.26 (.13)**	.04 (.17)	.11 (.11)	-.15 (.3)
Poison pill	-.42 (.18)**	-.35 (.11)**	-.07 (.14)	.06 (.12)	.22 (.22)
Banks & insurance cos	5.2 (2.2)**	1.3 (1.0)	-3.9 (1.8)**	.86 (.64)	4.0 (3.0)
Mutual funds	2.1 (.1.3)	1.7 (.76)**	-.6 (1.0)	1.1 (.89)	2.4 (2.1)
Ind investment advisors	1.6 (1.8)	.81 (.64)	-.77 (1.5)	1.3 (1.1)	-1.0 (2.5)
Other institutions	1.2 (1.6)	-1.5 (1.4)	-.22 (2.3)	6.6 (1.7)**	9.9 (4.0)**
Banks& insurance*after	-7.0 (3.5)*	-.79 (1.7)	2.2 (2.2)	-.8 (1.0)	-6.0 (3.4)*
Mutual funds*after	-2.5 (1.8)	.87 (1.2)	.56 (1.3)	.56 (1.4)	2.4 (3.1)
Ind invt advisors*after	-2.1 (2.1)	.37 (.9)	2.7 (2.0)	1.0 (1.4)	.65 (3.6)
Other*after	-2.7 (2.2)	-.35 (1.7)	-1.4 (2.8)	-2.9 (2.0)	-5.3 (4.1)
R2	.2275	.3038	.1555	.4294	.4219
# of observations	154	140	136	180	114

**Table 6. Mutual Fund Voting and Ownership after the Vote Disclosure Rule**

The table reports the average percentage of mutual funds' actual votes, and the votes of all investors, in support of proposals submitted as of the effective date of the mutual fund vote disclosure rule (July 1, 2003) by proposal type, for the firms for which we are able to obtain mutual fund data, and the t-statistic for the difference in mean between those votes calculated pairwise, \*\* means significant at less than 5 percent and \* means significant at 10 percent. The final two columns report, respectively, the average percentage of mutual funds (weighted by fund shares) holding stock in the firm at the time of the 'before' proposal that also hold the firm's stock at the time of the 'after' proposal (referred to as the funds' 'continued ownership'), and the same calculation of percentage of continued ownership for only the mutual funds for which we collected actual votes. Votes are collected for all equity mutual funds whose holding in the proposal firm's stock equals at least 0.75 percent of the fund's stock portfolio, or if that cutoff resulted in collecting votes for less than 1/3 of a proposal firm's holdings by mutual funds, then votes were collected for all equity mutual funds whose holdings in the firm were 0.25 percent of the fund's stock portfolio. Standard deviations of the percent continued ownership are given between parentheses. N/A means statistic not applicable.

<b>Proposal Type</b>	<b># of proposals</b>	<b>Mutual fund votes for</b>	<b>Votes for</b>	<b>T-stat difference in mean</b>	<b>Percent Continued ownership, all funds</b>	<b>Percent Continued ownership, funds with votes</b>
<i>Management proposals:</i>						
Common stock issuance	59	81.4	80.4	-0.4	.3532 (.23)	.1717 (.19)
Misc.	8	100	93	-1.7	.4339 (.25)	.1442 (.16)
Remove defenses	3	100	78.4	-3.5	.5958 (.11)	.2712 (.11)
EEIC	362	72.7	75.6	2.3**	.3532 (.23)	.1674 (.18)
Outside director equity incentive plan	32	75.9	80	1	.3623 (.26)	.1845 (.19)
Employee stock purchase plan	70	91.4	92	0.4	.3455 (.2)	.1561 (.16)
Bonus plan	63	93	92.3	-0.8	.3590 (.22)	.1617 (.16)
<i>Shareholder proposals:</i>						
Takeover defenses	90	84.7	59.9	-11.3**	.4558 (.26)	.1946 (.16)
Executive compensation	55	29.7	37.8	2.4**	.5296 (.24)	.1632 (.14)
Board independence	16	4.7	22.3	5.2**	.5889 (.28)	.1976 (.18)
Director elections	1	0	9.7	N/A	.7439 (N/A)	.4694 (N/A)
Misc.	14	9.4	20.5	3.5**	.4267 (.28)	.2065 (.18)

**Table 7. Mutual Fund Characteristics by Proposal Type**

This table provides information on the mutual fund characteristics of funds holding the firms with management-sponsored EEIC proposals (panel A) and shareholder-sponsored proposals on takeover defenses (panel B), and the holdings of the five largest fund families for the proposal firms, over the entire sample time period, and also for the individual mutual fund characteristics, the average values before and after the mutual fund vote disclosure rule's effective date (July 1, 2003) and the t-statistic for the difference in mean between the variables before and after calculated pairwise; \*\* means significant at less than 5 percent and \* means significant at 10 percent. Load is the sum of maximum front and rear loads.

**Panel A. Management Executive Incentive Compensation Plan Proposals (362 pairs)**

<b>Fund Characteristic</b>	<b>Average of funds</b>	<b>Standard deviation of funds</b>	<b>Average of funds as of before proposals</b>	<b>Average of funds as of after proposals</b>	<b>T-stat difference in mean</b>
Expense ratio	0.01	.002	0.01	0.01	1.6
Turnover ratio	0.65	.25	0.7	0.59	8.1**
Load	0.02	.02	0.02	0.02	2.6**
Maximum Front load	0.02	.01	0.02	0.01	5.6**
Maximum Rear load	0.005	.02	0.006	0.005	0.9
Total Net Assets (millions)	9,120	8,426	7,304	10,937	-10.3**
<b>Fund Family Holdings</b>					
Fidelity fund family	.019	.029			
Vanguard fund family	.011	.014			
Capital research fund family	.009	.021			
T. Rowe Price fund family	.006	.015			
Putnam fund family	.004	.009			

**Panel B. Shareholder Proposals on Takeover Defenses (90 pairs)**

<b>Fund Characteristic</b>	<b>Average of funds</b>	<b>Standard deviation of funds</b>	<b>Average of funds as of before proposals</b>	<b>Average of funds as of after proposals</b>	<b>T-stat difference in mean</b>
Expense ratio	0.01	.001	0.01	0.0096	3.7**
Turnover ratio	0.6	.22	0.65	0.55	4.2**
Load	0.03	.01	0.02	0.03	-3.1**
Maximum Front load	0.02	.01	0.02	0.02	-2.3**
Maximum Rear load	0.007	.003	0.007	0.008	-4.0**
Total Net Assets (millions)	12,036	8,963	8,121	15,951	-8.8**
<b>Fund Family Holdings</b>					
Fidelity family fund	.012	.02			
Vanguard family fund	.005	.008			
Capital Research family fund	.008	.024			
Dodge & Cox family fund	.004	.016			
Putnam family fund	.005	.01			

**Table 8. Predicting Mutual Fund Votes: Regressions of Fund Votes on Fund Characteristics**

The table reports the results of the regressions of actual mutual fund votes for all management-sponsored (MP) EEIC proposals (column 1) and for all shareholder-sponsored (SP) proposals on takeover defenses (column 2), submitted as of the mutual fund vote disclosure rule's effective date (July 1, 2003), for which mutual fund characteristics were available, on fund characteristics (averaged for the proposal firms). For a description of the variables see Tables 3 and 7; <sup>+</sup> indicates the variable value was adjusted by subtracting the sample annual mean. The dependent variable is the percent of mutual funds voting for the proposal. Robust standard deviations are given between parentheses, \*\* means significant at less than 5 percent and \* means significant at 10 percent. N/A means variable not applicable.

Variable	MP: EEIC	SP: Takeover Defenses
Expense ratio <sup>+</sup>	23.5 (14.5)	-42.9 (46.6)
Turnover ratio <sup>+</sup>	-.19 (.09)**	.20 (.20)
Ln(Total net assets) <sup>+</sup>	.02 (.03)	-.19 (.07)**
Load <sup>+</sup>	.01 (.23)	11 (4.9)**
Fidelity fund family	.09 (.53)	.97 (1.6)
Vanguard fund family	1.4 (1.3)	2.5 (2.5)
Capital Research fund family	1.3 (.65)**	.78 (.82)
T. Rowe Price fund family	1.7 (1.0)*	N/A
Dodge & Cox fund family	N/A	2.0 (1.1)*
Putnam fund family	-3.5 (1.4)**	-2.1 (2.4)
Return (-12)	1.3 (.54)**	.14 (1.3)
NPM	.32 (.17)*	.09 (.46)
ROA	-.29 (.21)	1.0 (.67)
Blank check preferred	-.08 (.05)	-.18 (.11)
Classified board	.02 (.03)	.08 (.08)
Special meeting restr.	-.01 (.03)	.17 (.07)**
Written consent restr.	-.03 (.03)	-.01(.07)
Poison pill	.02 (.03)	.01 (.05)
Confidential voting	-.01 (.05)	.03 (.06)
Constant	.75 (.06)**	.73 (.13)**
Regression F-statistic	2.06**	2.99**
R2	.0770	.3383
# of observations	362	90

**Table 9. Regressions of Votes for Using Expected Fund Votes**

The table reports the pooled panel regression results for voting outcomes of all management-sponsored (MP) EEIC proposals (columns 1-3) and for all shareholder-sponsored (SP) takeover defense proposals (columns 4-5), for all firms with proposal pairs, thus one proposal before and one after the mutual fund vote disclosure rule's effective date. For a description of the variables, see Table 3; 'Total mutual fund vote' is the estimated total vote by mutual funds (the percentage of mutual fund holdings multiplied by the predicted voting outcome from the regressions of actual mutual fund votes on mutual fund characteristics reported in Table 8, taking the estimation risk into account by bootstrapping the first-stage residuals and adding those to the fitted values of the expected fund vote); '\*aft' indicates an interaction between the variable and an 'after' dummy variable indicating that the proposal was adopted as of the rule's effective date. Robust standard deviations are given between parentheses, \*\* means significant at less than 5 percent and \* means significant at 10 percent.

Variable	MP: EEIC			SP: Takeover Defenses	
	(1)	(2)	(3)	(4)	(5)
Constant	1.3 (.35)**	1.2 (.41)**	.53 (.83)	-.41 (.83)	.15 (.73)
After	-.32 (.13)**			-.15 (.34)	
Percent same	-.06 (.16)	-.07 (.16)	-.45 (.30)	-.05 (.25)	.20 (.23)
Ln(Market cap)	.06 (.02)**	.07 (.03)**	.14 (.06)**	-.03 (.05)	-.09 (.04)**
Return (-12)		-.80 (.88)	-3.4 (1.6)**		-.23 (1.9)
Beta (-60)	.10 (.32)	.12 (.32)	-.43 (.64)	-.45 (.40)	-.92 (.36)**
Market return (-12)	-.66 (2.4)	.03 (2.4)	.14 (4.5)	.50 (6.2)	4.9 (4.8)
Turnover (-12)	-.13 (.02)**	-.14 (.02)**	-.16 (.05)**	-.19 (.07)**	-.16 (.09)*
ROA		-.84 (.46)*	-1.5 (1.1)		.12 (.75)
NPM		.62 (.35)*	1.5 (.62)**		.78 (.82)
Confidential voting		-.15 (.09)*	-.28 (.17)		.19 (.10)*
Blank check preferred		-.15 (.12)	.14 (.18)		-.29 (.23)
Classified board		.07 (.06)	.27 (.12)**		.38 (.11)**
Special meeting restr.		-.02 (.06)	-.24 (.11)**		.39 (.12)**
Written consent restr.		.03 (.06)	-.003 (.11)		.11 (.10)
Poison pill		-.18 (.06)**	-.13 (.12)		.06 (.11)
Banks & insurance cos	-.61 (.52)	-.19 (.65)	.18 (1.2)	.68 (.64)	.91 (.58)
Banks & insurance*after		-.82 (.73)	-.90 (1.3)		-.71 (.82)
Total mutual fund vote	-1.6 (.52)**	-1.36 (.58)**	-.13 (.78)	2.1 (.90)**	.87 (.85)
Total mutual fund vote *after	1.6 (.74)**	1.47 (.72)**	.40 (1.4)	.83 (1.4)	1.2 (1.2)
Ind investment advisors	-.48 (.30)	-.06 (.42)	-1.1 (.66)	2.6 (.75)**	1.3 (.93)
Ind invt advisors*after		-.57 (.53)			1.1 (1.1)
Other institutions	-1.1 (.51)**	-.72 (.81)	.65 (.96)	4.5 (1.1)**	6.9 (1.6)**
Other*after		-.30 (.90)			-3.1 (1.8)
Indep. directors stock			1.6 (2.8)		
Inside directors stock			-.31 (.81)		
Number directors			-.05 (.02)**		
Pct bd independent			-.42 (.33)		
Indstk*Total mutual fund vote *after			149 (50)**		
Indstk*Banks&insur*after			29.4 (45.4)		
Indstk*InvtAdv*after			53.3 (24)**		
Indstk*Other*after			-134 (37)**		
R2	.1484	.1703	.2504	.2733	.4363
# of observations	724	724	226	180	180

**Table 10. - Differences between Original Firms and Matches**

This table presents the mean difference (standard deviations are given between parentheses) between the original firms and the matched firms, (1) for ‘before’ proposals (proposals voted on before July 1, 2003), using the actual proposal dates for both original and matched firms in ‘Mean difference before (i)’; (2) for ‘before’ proposals, using the proposal dates for the original firms for both the original and the matched firms in ‘Mean difference before (ii)’; and (3) for ‘after’ proposal dates (using the dates of the original firms’ proposals voted on after June 30, 2003), and the difference-in-difference. The last column provides the number of matched pairs without any missing information for the difference-in-difference calculation. For a description of the variables see Table 3.

	<b>Mean diff. before (i)</b>	<b>Mean diff. before (ii)</b>	<b>Mean diff. after</b>	<b>Difference- in-difference</b>	<b># matched pairs</b>
Before voting outcome	-.0224** (0.010)				254
Ln(Market cap)	0.1956 (1.26)	0.3005 (2.17)**	0.4019 (3.00)**	0.1483 (2.37)**	254
Return(-12)	-0.0036 (0.98)	0.0120 (0.99)	0.0011 (0.44)	-0.0023 (0.51)	254
Beta(-60)	-0.0089 (0.87)	-0.0036 (0.39)	0.0130 (1.65)	0.0177 (2.03)**	254
Market return(-12)	-0.0037 (2.51)**	0.0013 (0.05)	-0.0003 (0.41)	-0.0003 (0.16)	254
Turnover(-12)	0.2302 (1.59)	0.1748 (1.43)	0.3128 (3.10)**	0.1131 (1.29)	254
Confidential voting	0.0722 (2.04)**	0.0273 (0.94)	0.0382 (1.27)	0.0118 (0.91)	254
Blankcheck Preferred	-0.0298 (1.06)	0.0234 (0.88)	0.0267 (1.07)	0.0000 (0.00)	254
Classified board	-0.0298 (0.66)	0.0313 (0.72)	-0.0038 (0.09)	-0.0276 (1.40)	254
Special meeting restr.	-0.0851 (1.89)*	0.0703 (1.61)	0.0496 (1.14)	-0.0236 (0.80)	254
Written consent restr.	-0.0596 (1.31)	0.0039 (0.09)	0.0038 (0.09)	0.0039 (0.15)	254
Poison pill	-0.0170 (0.37)	-0.0078 (0.18)	0.0115 (0.27)	0.0236 (0.78)	254
ROA	0.0128 (1.73)*	0.0069 (0.93)	0.0069 (1.12)	-0.0005 (0.07)	236
NPM	0.0153 (1.298)	0.0302 (1.71)*	0.0134 (0.92)	-0.0163 (0.75)	236
Ind directors stock	-0.0052 (1.84)*	0.1929 (0.75)	0.0699 (0.38)	0.1513 (0.40)	78
Inside directors stock	0.0503 (1.69)	-1.6157 (1.22)	-1.7530 (1.69)	-0.6026 (0.63)	78
Banks & insurance cos	-0.0038 (0.60)	.01777 (3.64)**	.0169 (2.95)**	-0.0004 (0.08)	259
Mutual Funds	-0.0110 (1.23)	0.0138 (1.69)	0.0324 (4.14)**	0.0196 (2.61)**	259
Ind investment advisors	-0.0282 (3.13)**	0.0239 (2.76)**	0.0041 (0.49)	-0.0194 (2.67)**	259
Other institutions	-0.0134 (2.29)**	0.1023 (0.77)	0.0004 (0.07)	0.0037 (0.60)	259
Date of before vote (difference in months)	-3.05 (1.60)				259

**Table 11. Votes Before for Both Originals and Matches: EEIC Proposals**

The table reports the pooled panel regression results of the voting outcome for all EEIC proposals for which we could find matches, using only the 'before' proposals for firms with proposal pairs (with one proposal before and one after the mutual fund vote disclosure rule's effective date of July 1, 2003), and also using the 'before' proposals of their matched firms. For a description of the variables, see Table 3; 'O\*' indicates an interaction with an 'original' dummy variable indicating that the firm also has a proposal after the rule's effective date. Robust standard deviations are given between parentheses.

Variable	(1)	(2)	(3)
Constant	.72 (.51)	.70 (.52)	.78 (.54)
Original	.07 (.08)	.16 (.32)	
Ln (Market cap)	.07 (.04)**	.07 (.04)**	.07 (.04)**
Return (-12)	-2.5 (1.2)**	-2.59 (1.2)**	-1.74 (1.79)
Beta(-60)	.39 (.35)	.42 (.35)	.48 (.51)
Market return (-12)	2.54 (2.6)	2.18 (2.7)	-1.72 (4.5)
Turnover(-12)	-.11 (.04)**	-.11 (.04)**	-.06 (.05)
ROA	-.32 (.91)	-.28 (.95)	.06 (1.37)
NPM	.16 (.51)	.13 (.53)	-.27 (.98)
Confidential voting	-.19 (.13)	-.20 (.13)	-.30 (.22)
Blank check preferred	.01 (.17)	.01 (.17)	-.07 (.21)
Classified board	.11 (.09)	.11 (.09)	.10 (.09)
Special meeting restr.	-.16 (.09)*	-.16 (.09)*	-.10 (.14)
Written consent restr.	.09 (.09)	.09 (.09)	.17 (.14)
Poison pill	-.05 (.09)	-.05 (.09)	-.008 (.14)
Banks & insurance cos	.30 (.79)	.69 (1.05)	.45 (1.09)
Mutual funds	-2.0 (.49)**	-2.31 (.68)**	-2.39 (.69)**
Ind investment advisors	.51 (.51)	1.02 (.80)	1.07 (.82)
Other institutions	-.58 (.85)	-1.41 (1.24)	-2.47 (1.35)*
O*Return (-12)			-2.36 (2.26)
O*Beta(-60)			-.09 (.73)
O*Market return (-12)			6.93 (5.7)
O*Turnover(-12)			-.12 (.07)*
O*ROA			-.62 (1.8)
O*NPM			.48 (1.2)
O*Confidential voting			.06 (.26)
O*Blank check preferred			.16 (.26)
O*Special meeting restr.			-.08 (.18)
O*Written consent restr.			-.13 (.19)
O*Poison pill			-.12 (.19)
O*Banks & insurance cos		-.78 (1.35)	-.32 (1.4)
O*Mutual funds		.57 (.86)	1.13 (.91)
O*Ind investment advisors		-.89 (1.02)	-.74 (1.04)
O*Other institutions		1.33 (1.56)	3.12 (1.65)*
R2	.1538	.1580	.1772
# of observations	400	400	400



**Table 12. Probability of Not Having a Management-sponsored EEIC Proposal after the Rule Change**

This table presents the results for two logit estimations of the likelihood of having no EEIC proposal after the mutual fund vote disclosure rule's effective date (July 1, 2003), for the sample of original firms (firms with both 'before' and 'after' proposals) and their matches (firms with a 'before' but no 'after' proposal). For a description of the variables see Table 3; 'voting outcome\_0' is the percentage of votes for the 'before' proposal; 'Months since before vote' is the number of months between the original firm's 'before' and 'after' proposals. All variables with an underscore '\_0' are level variables, with values as of the date of the original firm's proposal before the rule change, and all variables starting with 'd\_' are differences, calculated as the change in value from the original firms' 'before' proposal date to the original firm's 'after' proposal date. Robust standard deviations are given between parentheses.

Variable	(1)	(2)
Voting outcome_0	.008 (.009)	.007 (.009)
Months since before vote	.02 (.008)**	.014 (.009)
Ln(market cap)_0	-0.046 (0.09)	.007 (0.10)
Return(-12)_0	1.05 (5.46)	-.76 (5.67)
Beta(-60)_0	0.69 (1.31)	1.46 (1.41)
Market return(-12)_0	21.8 (15.8)	17.7 (16.4)
Turnover(-12)_0	-0.14 (0.10)	-0.11 (0.11)
Confidential voting_0	-0.23 (0.32)	-0.39 (0.33)
Blank check preferred_0	-0.44 (0.37)	-0.41 (0.39)
Classified board_0	-0.05 (0.22)	.07 (0.24)
Special meeting restr._0	-0.34 (0.23)	-0.39 (0.25)
Written consent restr._0	0.15 (0.23)	0.10 (0.24)
Poison pill_0	0.11 (0.24)	0.18 (0.25)
ROA_0		2.58 (2.43)
NPM_0		-2.40 (1.21)**
Banks & insurance cos_0	-6.29 (2.47)**	-5.31 (2.60)**
Mutual funds_0	-2.46 (1.39)*	-2.53 (1.48)*
Ind investment advisors_0	-0.14 (1.30)	.35 (1.45)
Other institutions_0	-.16 (2.64)	1.23 (2.91)
d_ln(market cap)	-0.34 (0.18)*	-0.25 (0.21)
d_return(-12)	0.29 (4.31)	-1.04 (4.50)
d_beta(-60)	-2.61 (1.32)**	-2.12 (1.37)
d_market return(-12)	4.59 (12.8)	6.82 (13.4)
d_turnover(-12)	-0.17 (0.14)	-0.16 (0.15)
d_confidential voting	-0.16 (0.74)	-0.29 (0.73)
d_blank check preferred	0.31 (0.74)	0.42 (0.75)
d_classified board	0.45 (0.50)	0.57 (0.51)
d_special meeting restr.	0.31 (0.33)	0.16 (0.34)
d_written consent restr.	-0.10 (0.39)	-0.07 (0.40)
d_poison pill	-0.45 (0.34)	-0.53 (0.37)
d_ROA		.26 (2.48)
d_NPM		-.54 (.95)
d_banks & insurance cos	-2.43 (2.38)	-.99 (2.55)
d_mutual funds	-4.00 (1.48)**	-3.36 (1.60)**
d_ind investment advisors	2.00 (1.47)	2.88 (1.59)*
d_other institutions	.57 (1.86)	1.13 (2.06)
Constant	2.47 (1.68)	.99 (1.84)
# observations	496	446
Pseudo R2	0.0974	0.0882

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