

*University of Pennsylvania, Institute for Law & Economics Research
Paper No. 11-28*

NYU Law and Economics Research Paper No. 11-29

Voting Through Agents: How Mutual Funds Vote on Director Elections

Stephen J. Choi

New York University (NYU) - School of Law

Jill E. Fisch

University of Pennsylvania Law School - Institute for Law and
Economics

Marcel Kahan

New York University (NYU) - School of Law

Voting Through Agents: How Mutual Funds Vote on Director Elections

Stephen Choi^{*}
Jill Fisch^{**}
Marcel Kahan^{***}

^{*} Murray and Kathleen Bring Professor of Law, New York University School of Law.

^{**} Perry Golkin Professor of Law, University of Pennsylvania Law School.

^{***} George T. Lowy Professor of Law, New York University School of Law. We are grateful to Heidi Stam for helpful comments.

Abstract

Shareholder voting has become an increasingly important focus of corporate governance, and mutual funds control a substantial percentage of shareholder voting power. The manner in which mutual funds exercise that power, however, is poorly understood. In particular, because neither mutual funds nor their advisors are beneficial owners of their portfolio holdings, there is concern that mutual fund voting may be uninformed or tainted by conflicts of interest. These concerns, if true, hamper the potential effectiveness of regulatory reforms such as proxy access and say on pay. This article analyzes mutual fund voting decisions in uncontested director elections. We find that mutual funds use a variety of strategies to economize on the costs of making voting decisions, including having funds in the same fund family vote in lockstep, voting virtually always in accordance with management recommendations, and voting virtually always in accordance with recommendations of ISS. Smaller fund families employ these strategies to a greater extent than larger families.

We further adduce evidence on how ISS recommendations affect fund voting. Funds that account for less than 10% of the assets in our sample exhibit a strong tendency to follow ISS recommendations, a much smaller percentage than funds that virtually always follow management recommendations (approximately 25% of assets). A much larger percentage (36% of the assets) votes in accordance with ISS withhold recommendations in approximately 50% of the cases. We conclude that the influence of ISS is due more to funds' measured evaluation of the ISS recommendations rather than to funds blindly following these recommendations.

We find no evidence that funds in families that are affiliated with commercial banks, investment banks, or insurance companies have a stronger proclivity than independent funds to vote in accordance with management recommendations or to shield their votes from criticism in order to maintain good business relations or generate new business for their affiliates.

The largest fund families – Vanguard, Fidelity, and American Funds, each of which individually accounts for roughly 11% of total mutual fund assets – vote substantially differently both from each other and from ISS recommendations. This is strong evidence of heterogeneity in the voting behavior of mutual funds in director elections.

Finally, we examine the factors associated with high (in excess of 30%) withhold votes in director elections. An ISS withhold recommendation, in conjunction with at least one of four factors – a withhold vote by Fidelity, the director missing 25% of board meetings, the company having ignored a shareholder resolution that received majority support, and a Vanguard withhold vote on outside directors with business ties to the company – is associated with a 49% probability of receiving a high withhold vote. Directors in these groups account for 48% of all directors who received high withhold votes. By contrast, an ISS withhold recommendation that is not combined with one of these factors is associated with only a 21% probability of a high withhold vote, and the general probability of a high withhold vote is a mere 2%. These findings suggest steps that companies and directors should take to try to avoid high withhold votes. They are also evidence that not all ISS recommendations have the same impact on voting outcomes.

Introduction

The recent trend in corporate governance is to empower shareholders by letting them vote on more issues and according these votes greater weight. In the last decade, shareholders have more frequently exercised their voting power to adopt or request corporate governance changes such as the elimination of staggered boards and the repeal of poison pills.¹ Companies increasingly heed these requests.² Investors have also persuaded many large public corporations to adopt majority voting provisions.³ Even in companies that lack majority voting, shareholders are using withhold vote campaigns to express dissatisfaction with firm performance and a growing number of issuers whose directors receive high withhold votes are taking steps to address shareholder concerns.⁴ The New York Stock Exchange amended its rules to eliminate discretionary broker voting in uncontested elections, effectively increasing the power of shareholders who cast a vote.⁵ Delaware, home to the majority of publicly traded corporations, amended its state corporation law in 2009 to authorize both proxy access bylaws and bylaws permitting reimbursement of shareholders' proxy solicitation expenses.⁶ The Dodd-Frank Act⁷ required that shareholders of public companies be given the opportunity to cast an advisory vote on executive compensation ("Say on Pay")⁸ and authorized the SEC to adopt rules granting

¹ See, e.g., Lucian A. Bebchuk, Alma Cohen, and Charles C.Y. Wang, Staggered Boards and the Wealth of Shareholders: Evidence from a Natural Experiment, working paper at 3 (2010), avail. at <http://ssrn.com/abstract=1706806> (describing increasing institutional investor opposition to staggered boards and efforts to dismantle existing staggered boards).

² See Marcel Kahan & Edward Rock, Embattled CEOs, 88 Texas L. Rev. 987 (2010).

³ See, e.g., Sarah Johnson, In the Minority on Majority Voting, CFO.com, Jan. 27, 2011, avail. at <http://www.cfo.com/article.cfm/14552148/?f=rsspage> (reporting that investors supported majority voting in over half the companies that held a vote on the issue in 2010, and that 70% of S&P 500 companies currently have majority voting).

⁴ Quinton Huckleby, Elections that Matter: A Review of Director Votes in 2008, Proxy Governance (2008), avail. at <http://www.directorsandboards.com/DBEBRIEFING/November2008/AReviewofDirectorVotesin2008FINAL.pdf>; Marcel Kahan & Edward Rock, The Insignificance of Proxy Access, forthcoming Virginia Law Review (2011) (showing that most companies rectify the problem that lead to the majority withhold vote).

⁵ See Stephen Choi, Jill Fisch & Marcel Kahan, the Power of Proxy Advisors: Myth or Reality?, 59 Emory L.J. 869, 873-74 (2010) (describing the rule change and its significance).

⁶ See 8 Del. C. § 112 (2009) (authorizing proxy access bylaws); 8 Del. C. § 113 (2009) (authorizing bylaws that provide for reimbursement of shareholder proxy solicitation expenses).

⁷ See Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

⁸ See id. § 951.

shareholders the right to have their nominees for the board of directors appear in the issuer's proxy statement ("Proxy Access").⁹

The potential effectiveness of shareholder voting depends critically on the manner in which mutual funds exercise their voting power. Mutual funds constitute the largest group of institutional investors, holding approximately 27% of the equity of U.S. public companies, and their ownership percentage is growing.¹⁰ Unlike most individual investors, mutual funds have the scale and sophistication that permits them to acquire information on their portfolio companies. And unlike other groups of institutional investors, mutual funds are relatively free of conflicts of interest.¹¹ Their voting decisions therefore are of particular significance.¹²

This being said, mutual funds are intermediaries – holders of pooled investments in which those with an economic interest, the fund shareholders, lack voting authority¹³ – and mutual fund voting decisions are thus made by agents, either the mutual fund board or the fund officers employed by the fund's investment advisor.¹⁴ Commentators have raised several concerns about this arrangement.¹⁵ Initially, commentators worried that mutual funds were not exercising independent judgment in voting their shares but either voting in favor of management or following the so-called "Wall Street Rule" and selling their stock when unhappy with

⁹ See *id.*, § 971. The SEC adopted a proxy access rule, SEC Rule 14a-11, 17 CFR 240.14a-11(2010), but the D.C. Circuit invalidated the rule based on the SEC's failure adequately to assess its costs and benefits. See *Business Roundtable v. SEC*, 2011 U.S. App. LEXIS 14988 (D.C. Cir. 2011).

¹⁰ See *Inv. Co. Inst.*, 2011 Investment Company Fact Book, at 12, avail. at www.ici.org/pdf/2011_factbook.pdf.

¹¹ But see notes ___ through ___ *infra* and accompanying text (discussing potential mutual fund conflicts of interest).

¹² See, e.g., Alan R. Palmiter, *Mutual Fund Voting of Portfolio Shares: Why Not Disclose?*, 23 *Cardozo L. Rev.* 1419, 1421 (2002) (explaining that mutual funds have become "the swing vote in U.S. corporate governance").

¹³ See Jennifer S. Taub, *Able but not Willing: The Failure of Mutual Fund Advisers to Advocate for Shareholder Rights*, 34 *Iowa J. Corp. L.* 843 (2009) (describing this intermediation).

¹⁴ Both the fund's board and its investment advisor owe fiduciary duties to the fund in exercising their power to make voting decisions. See, e.g., *Disclosure of Proxy Voting Policies and Proxy Voting Records By Registered Management Investment Companies*, Investment Company Act Release No. 25922, 17 C.F.R. 239, 249, 270, 274 (Jan.31, 2003) (explaining that investment advisor's fiduciary duty to the fund "extends to all functions undertaken on the fund's behalf, including the voting of proxies relating to the fund's portfolio securities."); *Jones v. Harris Assocs. L.P.*, 130 S. Ct. 1418 (2010) (explaining role and duties of mutual fund directors).

¹⁵ In addition to the concerns addressed in the text, some critics argued that mutual funds were not exercising their voting power in the best interests of the funds' shareholders. See, e.g., Palmiter, *supra* note ___; Mercer Bullard, *Are Ballots Too Secret? Fund Advisers Should Tell How They Vote Proxies*, at <http://www.thestreet.com/funds/mercerbullard/1240302.html> (Jan. 4, 2001).

management.¹⁶ More recently, critics have expressed concern over the influence of proxy advisors, especially Institutional Shareholder Services (“ISS”), the leading proxy advisor, and worried about the extent to which mutual funds directly or indirectly delegate their voting judgments to such advisors.¹⁷ Some executives claim that ISS is able to influence shareholder votes by 30% or more.¹⁸ As related by Delaware’s Chancellor Leo Strine, the primary concern is that “some institutional investors will simply follow ISS’s advice rather than do any thinking of their own.”¹⁹ Other commentators are concerned that mutual funds are influenced by the desire of fund advisers to obtain business for the banks or insurance companies that may be affiliated with the fund company or pension-related business for the fund company, a conflict that would lead mutual funds to follow management recommendations.²⁰

There is only limited empirical research on the manner in which mutual funds vote their shares and the extent to which they are influenced by the foregoing factors. This research to date can be divided into three groups. First, a series of articles considers the extent to which mutual funds favor management in voting on director elections, shareholder proposals, or both. In a contemporaneous study, Matvos and Ostrovsky find that the average director receives a 90% for vote from mutual funds.²¹ The authors also demonstrate consistency in voting patterns within fund families. Matvos and Ostrovsky document considerable heterogeneity among funds: some

¹⁶ See Alan Palmiter, *Mutual Fund Voting of Portfolio Shares: Why not Disclose?*, 23 *Cardozo L. Rev.* 1419, 1430-34 (2002) (discussing various explanations for mutual fund passivity); see also John C. Coffee, Jr., *Liquidity Versus Control: The Institutional Investor as Corporate Monitor*, 91 *Colum. L. Rev.* 1277, 1288 n. 29 (1991) (describing possible origin of the “Wall Street Rule”).

¹⁷ See, e.g., Stephen Choi, Jill Fisch & Marcel Kahan, *Director Elections and the Role of Proxy Advisors*, 82 *S. Cal. L. Rev.* 649, 658 (2008-2009) (describing concerns over the influence of ISS on institutional investor voting decisions).

¹⁸ See, e.g., Posting of William J. Holstein to BNET: The Corner Office, <http://blogs.bnet.com/ceo/?p=1100&tag=content;col1> (Feb. 7, 2008, 08:03) (30%); Paul Rose, *The Corporate Governance Industry*, 32 *J. Corp. L.* 887, 889 (2007) (attributing this view to executives). (“a third or more”)

¹⁹ See Leo E. Strine, Jr., *The Delaware Way: How We Do Corporate Law and Some of the New Challenges We (and Europe) Face*, 30 *DEL. J. CORP. L.* 673, 688 (2005).

²⁰ See, e.g., *Disclosure of Proxy Voting Policies*, supra note __, at 17 (explaining that fund’s investment advisor may face a conflict of interest in voting the securities of a portfolio company when the advisor “also manages or seeks to manage the [company’s] retirement plan assets.”)

²¹ See Gregor Matvos & Michael Ostrovsky, *Heterogeneity and Peer Effects in Mutual Fund Proxy Voting*, 98 *J. Fin. Econ.* 90, 95 (2010).

funds are consistently more likely to support management than others.²² At the same time, they document substantial peer effects, showing that a fund is significantly more likely to withhold its votes from a director candidate if its peers are expected to do so.²³ But Morgan, et al., challenge Matvos and Ostrovsky’s findings of consistency, at least within the context of shareholder proposals, establishing “substantial divergence across funds within the same family with respect to voting on shareholder proposals.”²⁴ Cremers and Romano analyze the effect of the 2003 SEC rule change that mandated disclosure of mutual fund votes.²⁵ Studying the votes on executive equity compensation plans, the authors find no evidence of decreased support for management and instead, evidence of increased management support. Ng, et al., find that mutual fund voting is related to prior firm performance.²⁶

Second, several articles look specifically at potential mutual fund conflicts of interest. These studies arrive at inconsistent results. Rothberg and Lilien find no significant difference in voting between four mutual fund companies and four other funds that are affiliated with financial services firms.²⁷ Davis and Kim examine funds that manage corporate pension funds and find no significant difference in their voting on portfolio companies whose pensions they manage and their voting on other portfolio companies.²⁸ They thus conclude that pension-related business influences voting decisions. In contrast, Jennifer Taub, studying the ten largest mutual funds, finds that a higher value of defined contribution plan assets under management for the fund’s

²² See id. at 96-97.

²³ See id. at 97.

²⁴ See Angela Morgan, Annette Poulsen, Jack Wolf, and Tina Yang, Mutual funds as monitors: Evidence from mutual fund voting, 17 *J. Corp. Fin.* 914 (2011).

²⁵ See K.J. Martijn Cremers & Roberta Romano, Institutional Investors and Proxy Voting on Compensation Plans: The Impact of the 2003 Mutual Fund Voting Disclosure Rule, *Am. L. & Econ. Rev.* (2011)

²⁶ See Lilian Ng, Qinghai Wang, & Nataliya Zaiats, Firm performance and mutual fund voting, 33 *J. Bank. & Fin.* 2207 (2009).

²⁷ See Burton Rothberg & Steven Lilien, Mutual Funds and Proxy Voting: New Evidence on Corporate Governance, 1 *J. Bus. & Tech. L.* 157 (2006).

²⁸ See Gerald F. Davis & E. Han Kim, Business Ties and Proxy Voting by Mutual Funds, 85 *J. Fin. Econ.* 552–70 (2007).

advisor is correlated with reduced support for shareholder proposals.²⁹ Similarly, Ashraf et al. find that mutual funds with pension-related business are less likely to support shareholder proposals on executive compensation.³⁰

Finally, a few studies examine the general influence of ISS on voting decisions. ISS is widely considered to be highly influential.³¹ Cai, et al. find that a negative ISS recommendation increases withhold votes in director elections by approximately 20%.³² By contrast, in an earlier article, we estimate that ISS swings only 6-10% of the vote in uncontested director elections.³³ Neither of these studies looks specifically at mutual fund voting. Cotter, Palmiter and Thomas examine voting on shareholder proposals and find that mutual funds³⁴ vote more consistently with ISS recommendations than with management recommendations.³⁵

In addition to academic studies, the Investment Company Institute has published various statistical analyses of mutual fund voting.³⁶ One recent report reveals that, although mutual funds have consistently supported management and management proposals, voting in favor of director nominees more than 90% of the time, this support has declined over the 2007-2009 time

²⁹ See Taub, *supra* note __.

³⁰ See Rasha Ashraf, Narayanan Jayaraman, & Harley E. Ryan, Jr., *Conflicts of Interest and Mutual Fund Proxy Voting: Evidence from Shareholder Proposals on Executive Compensation* (2009), avail.at http://69.175.2.130/~finman/Reno/Papers/Proxy_Vote_Paper_01082009.pdf; see also Rasha Ashraf, Narayanan Jayaraman, & Harley E. Ryan, *Do Pension-Related Business Ties Influence Mutual Fund Proxy Voting? Evidence from Shareholder Proposals on Executive Compensation* (November 23, 2010), avail.at <http://ssrn.com/abstract=1351966> (finding that this effect exists at both client and on-client portfolio companies).

³¹ See, e.g., Choi et al., *supra* note __ at 871 (describing claims of ISS's influence).

³² See Jie Cai, Jacqueline Garner & Ralph A. Walkling, *Electing Directors*, 64 J. Fin. 2389(2009).

³³ See Choi et al., *supra* note __. (Emory)

³⁴ The influence of ISS may differ with respect to other types of institutional investors such as public pension funds. See generally Stephen J. Choi & Jill E. Fisch, *On Beyond CalPERS: Survey Evidence on the Developing Role of Public Pension Funds in Corporate Governance*, 61 Vand. L. Rev. 315, 342 (2008) (describing delegation by public pension funds of voting authority and the preparation of voting guidelines).

³⁵ See James Cotter, Alan Palmiter, & Randall Thomas, *ISS Recommendations and Mutual Fund Voting on Proxy Proposals*, 55 Vill. L. Rev. 1 (2010).

³⁶ The Investment Company Institute, a membership organization, is the national association of U.S. investment companies, which include mutual funds as well as ETFs, closed-end funds and unit investment trusts. See Inv. Co. Inst., *About ICI*, http://www.ici.org/about_ici (last visited Aug. 4, 2011) (describing the ICI).

frame, largely due to fund concerns about executive compensation which have led to increased withhold votes for directors on board compensation committees.³⁷

Our study is the first to examine the relationship between ISS and mutual fund voting on director elections. Director elections differ significantly from votes on shareholders proposals because they are much more information intensive. Most funds have developed guidelines on how to vote on certain proposals (e.g., in favor of proposals to destagger the board and against proposals to split the chairman and CEO positions) which will determine most of their votes.³⁸ By contrast, director votes are more complex and funds are thus arguably more dependent on the information supplied by and the evaluation of ISS. Moreover, unlike prior studies, our study examines the extent to which voting by funds is explained by fund family size. Finally, our study is the first to examine the voting of the three largest mutual fund families – Vanguard, Fidelity, and American funds – which dominate the mutual fund industry³⁹ and the first to shed specific light on what causes directors to receive an embarrassingly high percentage of withhold votes.

Part I explains our methodology and the selection of our data sample. Part II examines the use by mutual funds of voting strategies that economize on the costs of voting. Specifically, we consider three strategies: centralized voting decisions by funds that are part of the same fund complex; voting in accordance with ISS recommendations; and voting in accordance with management recommendations. We find that mutual funds are heavy users of these economizing

³⁷ See Inv. Co. Inst., Trends in Proxy Voting by Registered Investment Companies, 2007–2009 (Nov. 2010).

³⁸ See, e.g.,

<https://personal.vanguard.com/us/content/Home/WhyVanguard/AboutVanguardProxyVotingGuidelinesContent.jsp>

(Vanguard proxy voting guidelines which state, among others, that Vanguard funds “will generally support proposals to declassify existing boards (whether proposed by management or shareholders) and will block efforts by companies to adopt classified board structures, in which only part of the board is elected each year.”)

³⁹ In our sample period, these three fund families accounted for 32% of all mutual fund assets. Data on mutual fund asset holdings as of March 31, 2007, provided by Mr. Erin H. Short, Senior Research Associate, Statistical Research, Investment Company Institute. See e-mail from Erin Short to Marcel Kahan dated May 17, 2007.

strategies, with small fund families being more likely to employ these strategies than large fund families.

Part III examines the relationship between mutual fund voting and ISS recommendations. We find that the percentage of assets managed by mutual funds that appear to follow ISS “blindly”, without, in Chancellor’s Strine’s words, “any thinking of their own,”⁴⁰ is small, around 3% to 8% of the assets of all the funds in our data sample (referred to as “sample assets”). Moreover, that percentage is significantly below the percentage of sample assets managed by funds that appear to follow management recommendations without any thinking of their own. But a much larger asset pool (36% of sample assets) votes in accordance with ISS withhold recommendations in approximately 50% of the cases. The influence of ISS is thus mostly due to funds’ measured evaluation of the ISS recommendations, with significant thinking on their own, rather than to funds’ blindly following these recommendations.

Part IV examines the voting by mutual fund families that are affiliated with other financial companies, such as banks or insurance companies. We do not find any significant evidence for the hypothesis that funds in these families vote in a manner designed to avoid alienating the management of portfolio companies in order to generate business for the fund affiliates.

Part V analyzes the voting behavior of the three largest mutual fund families: Fidelity, Vanguard and American. We find that these families base their voting decisions on different factors, both from each other and from the factors that affect ISS voting recommendations. Moreover, we find that ISS recommendations are more in tune with voter sentiments at large than with the voting decisions by these three fund families.

Finally Part VI considers the factors associated with high director withhold votes (which we define as a withhold vote of 30% or more of the votes cast). We identify four factors that,

⁴⁰ See supra note ____.

combined with an ISS withhold recommendation, significantly increase the probability of receiving a high withhold vote relative to an ISS withhold recommendation alone: a withhold vote by Fidelity, the director missing 25% of board meeting, the company having ignored a shareholder resolution that received majority support, and a Vanguard withhold vote on outside directors with business ties to the company. An ISS withhold recommendation, in conjunction with at least one of these factors is associated with a 49% probability of receiving a high withhold vote and directors in these groups account for 48% of all directors who received high withhold votes. By contrast, an ISS withhold recommendation not combined with one of these factors is associated with a 21% probability of receiving a high withhold vote, and the general probability of a high withhold vote is a mere 2%. These findings suggest steps that companies and directors should take to try to avoid high withhold votes. They are also evidence that not all ISS recommendations have the same impact on voting outcomes.

I. Methodology

To construct the data sample for this study, we selected fund families in three size categories as follows. We obtained a list of 348 mutual fund families from the Investment Company Institute with the amount of assets under management broken down between short-term and long-term assets as of March 31, 2007.⁴¹ We sorted this list by the amount of long-term assets. For the category of large funds, we chose the 20 fund families with the largest amount of long-term assets. The assets in this group ranged from \$88 billion to \$1,115 billion, with an average of \$275 billion and a median of \$136 billion. For medium-size families, we chose the 20 families with the largest amount of long-term assets below \$40 billion. The assets in this group ranged from \$39 billion to \$18 billion with an average of \$27 billion and a median of \$26 billion. For small families, we chose the 20 families with the largest amount of long-term assets below

⁴¹ See e-mail from Erin Short to Marcel Kahan, *supra* note ____.

\$10 billion. The assets in this group ranged from \$10 billion to \$5 billion with an average and median of \$7 billion.⁴²

For each fund family, we examined Form N-PX filings and tabulated the votes of all domestic equity funds of the sample families in uncontested director elections in 2005 and 2006 and the voting recommendations on these directors by ISS. We examined only elections at S&P 1500 companies, and we eliminated any fund that cast less than 100 votes in these elections, leaving us with 719 funds across the different fund families. Of the sixty families initially selected, 4 had to be eliminated because they had no funds that satisfied these criteria. For the remaining families, we obtained ownership information from securities filings and press report to determine whether they were affiliated with a financial institution in 2005 or 2006.

For each director vote, we collected data⁴³ from SEC filings and the IRRC Governance database on the following:(1) whether the director was the CEO (CEO), an employee of the company other than the CEO (Empl_Dir), an outside directors with certain links to the company (OutDirLink) or a new Director (New Director); (2) whether the director was member of the audit (AuditMbr), the compensation committee (CompMbr) or the nominating committee (NomMbr), and (3) whether the director was a member of at least three other “major” company boards during the year prior to the annual meeting date (ManyBds),⁴⁴ whether the director attended less than 75% of the director meetings (Attendance), whether the director was an Interlocking director (Interlock), and whether the director was 75 years or older (Age75). In addition, for each company in the sample and each year, we collected data from SEC filings, press releases, the IRRC Governance database, the Georgeson Annual Corporate Governance Reviews, and CRSP on (1) whether the first public report of a restatement to a company’s

⁴² Families for which no data were available on CRSP, who had no domestic funds, or who were affiliated with a larger fund family were eliminated and the family with the next lower long-term assets was chosen instead.

⁴³ For a definition of these and other variables, see the Appendix.

⁴⁴ We use the IRRC data on other “major” company boards held by directors for the year prior to the annual meeting.

financial statement occurred within two years prior to the annual meeting (Prior Restat), the first public statement of a SEC investigation or enforcement action occurred within two years prior to the annual meeting (Prior SEC), and the company rejected an issue proposal that had received majority shareholder support in the last year (IP No); (2) whether the company had a classified board (ClassBd), a poison pill (Poison Pill), cumulative voting (CumVote), or golden parachutes (Golden Parachute); and (3) whether the company was in the top or bottom 5% of the companies ranked based on abnormal holding period return for the three-year period prior to the meeting date for the year of the recommendation adjusted based on the CRSP value-weighted market index (Top5AbRet, Bot5Abret); and (4) whether the CEO for the company was in the top 5% total excess compensation (Top5AbComp).⁴⁵ We also obtained ISS's voting recommendation for each director from ISS or from LEXIS (VoteISS = 1 for a "withhold" recommendation and 0 for a "for" recommendation).

II. Centralization and Short Cuts

A. Centralization of Fund Voting

Most funds are separate legal entities. Moreover, different funds are generally run by different fund managers.⁴⁶ Technically, each fund has its own board of directors as well.⁴⁷ As a

⁴⁵ See also Stephen Choi, Jill Fisch & Marcel Kahan, Director Elections and the Role of Proxy Advisors, 82 S. Cal. L. Rev. 649 (2009); Choi, et al., supra note ____.

⁴⁶ For a general description of the legal structure of mutual funds see Jill E. Fisch, Rethinking the Regulation of Securities Intermediaries, 158 U. Penn. L. Rev. 1961, 1967 (2010).

⁴⁷ See 15 U.S.C. § 80a-10(a) (requiring mutual funds to have their own boards of directors or trustees whether or not they are structured as corporations). It is commonplace that the same individuals serve on the boards of many or all of the funds within a given fund family. The practice of having the same directors serve on the boards of multiple funds within a fund complex is known as the unitary board model. Comment Letter from Heidi Stam, Managing Director and General Counsel, Vanguard to Elizabeth Murphy, SEC, dated Aug. 18, 2009, avail. at www.sec.gov/comments/s7-10-09/s71009-326.pdf. This practice has been endorsed by most of the fund industry, and was recently acknowledged as the dominant industry model by the D.C. Court of Appeals. See Business Roundtable v. SEC, 2011 U.S. App. LEXIS 14988, *25 (D.C. Cir. 2011) (citing survey data showing that 81% of responding funds have a unitary board). As industry leader Vanguard explains: "unitary boards are powerful and efficient bodies, better able to moderate the influence of the advisers who operate the funds day-to-day." Id. at 2.

result, one might expect fund voting decisions to vary even for funds that are part of the same fund family.

Both the research and the mechanics of proxy voting are costly. In addition to the obvious operational costs, proxy voting decisions raise policy and strategic issues.⁴⁸ As a result, funds in the same fund family might instead economize on the costs associated with voting by delegating voting decisions to a single centralized body. We analyze the extent to which fund voting is centralized by examining the extent to which fund votes within a single fund family deviate from each other.

Within each fund family, we define separate clusters of funds that vote largely in lockstep with one another. We place a fund in a cluster if it votes in lockstep with the other funds in the cluster in director elections, i.e. if there are no or only a trivial number of deviations in the votes on the same nominees for the same company. Examining these clusters, we find that fund voting is often highly centralized, but that the degree of centralization varies by fund family. For purposes of this study, we classify a fund family as fully centralized if all funds in that family belong to a single voting cluster. We classify a family as substantially centralized if one group of funds in that family that accounts for at least 70% but less than 100% of the aggregate fund family assets votes in lockstep in director elections forming a single cluster. Fund families are classified as non-substantially centralized if no such single dominant cluster exists.

Several fund families could not be classified because the family consisted of a single fund or because the funds within that family had insufficient overlap in holdings to determine whether these funds voted in lockstep and the funds at issue accounted for a material portion of the aggregate fund family assets. In total, of the 56 families in our sample, we were able to classify

⁴⁸ In addition to the predicted impact of the issue for the portfolio company, a fund may have to consider its overall investment strategy as well as public perception and reputation. See, e.g., Laura Smitherman, T. Rowe Price takes activist role, Balt. Sun, June 8, 2007, avail. at http://articles.baltimoresun.com/2007-06-08/business/0706080254_1_rupert-murdoch-rowe-price-private-equity (describing media attention focused on T. Rowe Price after its money managers took activist positions with respect to several corporate buyouts).

38 families. Of these families, we find that 21 were fully centralized and another 12 were substantially centralized; only 5 were classified as non-substantially centralized. Even in fund families that were classified as non-substantially centralized, some of the funds voted in lockstep. For example, we classified the Blackrock fund family as non-substantially centralized. The 10 Blackrock funds in our sample formed three clusters: 5 funds voted in lockstep with each other, 4 others voted in lockstep with each other (and not in lockstep with the first cluster) and the last fund voted out of lockstep with the other two clusters, forming a third cluster.

In total, the 719 funds of the 56 families form 127 different clusters. For the remainder of our analysis, we treat several funds within the same family that vote in lock-step and form a cluster as a single fund: we aggregate their assets and, when multiple funds in a cluster cast votes on the same director-nominee, we treat them as a single observation.

In some instances, the reason why funds in the same family voted differently, or in different clusters, was apparent. For example, the current Franklin Templeton family consists of the (old) Franklin Templeton funds and the Mutual series of funds, formerly owned by Heine Securities Corporation, which merged into Franklin Templeton in 1996.⁴⁹ The funds that were formerly part of the Mutual series vote out of lockstep with the other Franklin Templeton funds, but in lockstep with each other. In the case of Fidelity, variation in fund voting has a different explanation. Fidelity index funds are sub-advised by Geode Capital Management LLC in order to avoid having their holdings aggregated with the holdings of other Fidelity funds for purposes of Section 13(d) of the Securities Exchange Act of 1934.⁵⁰ We find that the index funds vote out

⁴⁹ See Franklin Resources, Inc., Press Release, Franklin Resources Inc. Merges with Heine Securities Corporation (Nov. 1, 1996), avail. at https://www.franklintempleton.com/retail/pages/corp/press/1996/heine_110196.jsf?archived=true. (describing the merger).

⁵⁰ See 15 U.S.C. § 78m(d).

of lockstep with the other Fidelity funds, but this is explained by the fact that their voting decisions were intentionally separated from those of other Fidelity funds.⁵¹

In many other instances, however, no such ready explanations are available. In these cases, the portfolio managers of individual funds may exercise greater control of the fund voting. Also, in some instances, lack of overlap among the votes cast by different funds, due to the variation in fund holdings, prevented us from determining whether the funds voted in lockstep or not. These funds may, in fact, vote in lockstep with each other, but we lacked sufficient observations to determine so with confidence.

Centralization is more common among smaller fund families. As Table 1 shows, 83% of the small funds are fully centralized, while only 40% of the medium-sized and 44% of the large funds are fully centralized. In chi-square tests, the difference in centralization between large and small funds is statistically significant (Pearson $\chi^2(2) = 5.0613$ Pr = 0.080).⁵² The difference in degree of centralization may, to some extent, be due to the fact that larger families are more likely to have incorporated predecessor funds and retained multiple decision-making bodies within the overall fund family.

Table 1: Fund Family Size and Centralization

	Non-Substantially Centralized	Substantially Centralized	Fully Centralized	Total
Large	3	6	7	16
Medium	2	4	4	10
Small	0	2	10	12

⁵¹ See Special Report, Fidelity's Divided Loyalties, Bloomberg Businessweek, Oct. 16, 2006, http://www.businessweek.com/magazine/content/06_42/b4005060.htm

⁵² We also test the difference across all three types of funds and find that the difference is insignificant (Pearson $\chi^2(4) = 6.0785$; Pr = 0.193.).

B. Short-cuts

We next examine the extent to which funds rely on short-cuts to reduce the transaction costs associated with voting. The literature has raised two possible short-cuts that mutual funds may use: (1) virtually always following the voting recommendations by Institutional Investor Services (ISS)⁵³ and (2) virtually always following the voting recommendations of the board of directors (which means, in effect, voting “for” the board nominees).⁵⁴ The concern about both these short-cuts is that they frustrate the role of shareholder voting as a corporate governance mechanism: in neither case do funds engage in any thinking of their own. If funds routinely vote with management, shareholder voting is not operating as a constraint on managerial agency costs and leads to self-perpetuating boards. This concern is of particular significance in the context of director elections in that the shareholders’ ability to elect the board is a substantial protection against inadequate corporate performance and the intellectual foundation of board management powers and legal rules such as the business judgment rule.⁵⁵

The possibility that funds routinely follow ISS recommendations raises different issues. Many commentators have expressed concerns about the potential influence that ISS exercises over corporate elections, concern that we will explore in more detail below.⁵⁶ To the extent that mutual funds delegate their voting authority to ISS directly or indirectly by blindly following ISS recommendations, they are not exercising independent decision-making authority. Instead,

⁵³ See, e.g., Lynn A. Stout, *Why Should ISS Be The New Master Of The Corporate Governance Universe? CORPORATE GOVERNANCE*. (Dow Jones Financial Information Services, New York, N.Y.) Jan. 4, 2006, at 14 – 15 (describing how SEC regulation of mutual fund voting has driven mutual funds “into the arms of ISS”); Tamara C. Belinfanti, *The Proxy Advisory and Corporate Governance Industry: The Case for Increased Oversight and Control*, 14 *Stan. J.L. Bus. & Fin.* 384, 386 (2009) (stating that “15-20% of mutual funds have even authorized ISS to automatically vote their shares however it sees fit”).

⁵⁴ See, e.g., Palmiter, *supra* note __ (Cardozo).

⁵⁵ See, e.g., *Blasius Industries, Inc. v. Atlas Corp.*, 564 A.2d 651, 659 (Del. Ch. 1988) (“matters involving the integrity of the shareholder voting process involve consideration not present in any other context in which directors exercise delegated power.”).

⁵⁶ See, e.g., Belinfanti, *supra* note __.

significant power is granted by a single entity that holds no equity stake in portfolio companies and whose incentive structure on voting decisions is less than clear.

We first consider the extent to which funds appear to employ short-cut techniques. We view a fund as employing a pro-management short-cut rather than voting independently if the fund has a withhold rate that is less than one-tenth of the frequency of ISS withhold recommendations (the “relative withhold rate”) for the director nominees on which the fund voted (which amounts, on average, to an absolute fund withhold rate below 0.6%). We view a fund as employing an ISS-short-cut if the fund votes in accordance with the ISS recommendation in 99.5% or more of its votes. We will term these “primary short-cuts.”

Of the 127 clusters in our sample, 23 employ primary short-cuts: 10 virtually always follow ISS (ISS primary short-cut) and 13 virtually always follow the board recommendation (board recommendation primary short-cut). Of the remaining 104 clusters, 31 exhibit less strong voting patterns, as follows: 12 follow ISS “for” vote recommendations in at least 99.95% of the votes (but not ISS “withhold” vote recommendations to the same degree); 12 follow ISS “withhold” vote recommendations in at least 99.5% of the votes (but not ISS “for” vote recommendations to the same degree); 5 have a relative withhold rate below 0.2 on the director nominees on which the fund voted (indicating some deference to the board recommendation but not to the extent as those funds with a board recommendation primary short-cut); and an additional 2 funds vote according to the ISS recommendation in 99% or more of their votes. We describe these less pronounced patterns as “secondary short-cuts.” In total, 54 of the 127 clusters (42.5%) follow some sort of short-cut.

We next examine the relationship between the use of short-cuts and fund family attributes. For each fund family, we look at the largest fund cluster as measured by asset size. This approach generates 56 different clusters (termed the “dominant” clusters). Within this group of dominant clusters, 7 follow ISS in over 99.5% of its recommendations (ISS primary

short-cut) and 8 have a relative withhold rate of less than 0.1 (board recommendation primary short-cut). Many of the other dominant clusters used a secondary short-cut: 5 follow ISS “for” vote recommendations in at least 99.95% of the votes; 1 follows ISS “withhold” vote recommendations in at least 99.95% of the votes; 4 have a relative withhold rate below 0.2; and 2 more funds vote according to the ISS recommendation in over 99% of the votes.

Since there are significant economies of scale involved in arriving at an independent voting decision (i.e., not following a short-cut), we hypothesize that dominant clusters in larger fund families are less likely to use short-cuts than dominant clusters in smaller fund families. Our data confirm this hypothesis. Among small fund families, 12 of 18 used a short-cut, among medium sized of 10 of 19, but among large only 5 of 19. The difference in the proclivity to use short-cuts for fund families of different size is statistically significant (Pearson $\chi^2(2) = 4.9350$; $Pr = 0.085$).

III. Mutual Funds and ISS

As discussed above, ISS is widely viewed as extraordinarily powerful in influencing shareholder votes.⁵⁷ In our prior work, we tried to measure the impact of an ISS recommendation on voting outcomes and concluded that ISS is significantly less influential than commonly assumed. According to our estimates, an ISS recommendation swings 6-10% of the votes.⁵⁸

Our data here allow us to examine the influence of ISS from a different perspective. To the extent ISS has influence, it is likely to be predominantly exercised through the voting recommendations it makes to institutional investors that are its clients. Mutual funds are the most important segment of institutional investors and, among the larger segments, have been

⁵⁷ See note __ infra and accompanying text.

⁵⁸ See Choi et al., supra note __, at 906 (Emory).

growing the fastest. Our sample includes approximately 50% of the domestic equities held by mutual funds. An analysis of the extent to which ISS controls the votes of mutual funds in our sample will thus shed significant additional light on its overall influence.

Table 2 below gives some information on the assets and the percentage of the aggregate sample assets for funds that vote in accordance with ISS recommendations. Funds that follow ISS with respect to more than 99% of all ISS recommendations account for a mere 3% of the sample assets. Funds that follow ISS with respect to 97.5% of all ISS recommendations account for only 10% of the sample assets. Two caveats are important. First, we are measuring overlap, not causation. Second, most ISS recommendations are in favor of the director nominees, and most votes are cast in favor of the director nominees -- thus, a substantial degree of correspondence with ISS recommendation is less significant than it initially appears. A fund that always voted "for" regardless of the ISS recommendation would vote in accordance with the ISS recommendations in about 94% of all cases, even though such a fund's votes would presumably be completely independent of the ISS recommendation.

Because of the large percentage of ISS "for" recommendations and fund "for" votes, it is perhaps more valuable to examine "withhold" recommendations and votes. Here we find that, for funds accounting for 3.2% of the sample assets, the probability that they vote withhold if ISS recommended a withhold vote is at least 90% and for funds accounting for 8.07% of the sample assets, the corresponding probability is at least 80%. Similarly, in funds accounting for 7.06% of the sample assets, 90% or more of the withhold votes cast by the fund correspond to an ISS withhold recommendation, and in funds accounting for 13.27% of the sample assets, 80% or more of the withhold votes cast by the fund do so.

Given that funds may (and indeed are likely to) independently apply some of the same criteria as ISS in deciding how to vote, and that funds may consider ISS recommendations as one of several factors in deciding how to vote, we believe that cutoffs in the 80% to 90% range are

appropriate in assessing whether a fund follows ISS almost somewhat blindly or whether it applies substantial independent analysis.

Table 2: Fund Voting and ISS Recommendations

	Assets (\$ millions)	Percentage of Assets in sample
Fund Votes that Follow ISS >.99	76,632	3.04%
Fund Votes that Follow ISS > .975	255,874	10.16%
Fund Votes that Follow ISS > .95	478,701	19.00%
Fund WH votes conditional on ISS WH rec. > .9	80,664	3.20%
Fund WH votes conditional on ISS WH rec. > .8	203,345	8.07%
Fund WH votes conditional on ISS WH rec. > .7	208,719	8.28%
Fund WH votes that follow ISS/total Fund WH votes > .9	177,764	7.06%
Fund WH votes that follow ISS/total Fund WH votes > .8	334,244	13.27%

To put ISS’s influence in perspective, we compare the assets held by funds that have a strong tendency of following ISS with the assets held by funds that have adopted a “follow management” short-cut. Funds that have a relative withhold rate of less than 0.1, which translate roughly into an absolute withhold rate of 0.6% or less, account for 24% of the aggregate samples assets, and funds with a relative withhold rate of less than 0.2% account for 27% of the aggregate assets. Withhold rates this small presumably do not reflect much scrutiny of and independent judgment on the board nominee by the fund involved. To the extent withhold votes are supposed to serve as a shareholder check on the board, the voting behavior of these funds is unlikely to fulfill this purpose. Thus, at least for the mutual funds in our sample, excessive deference to ISS recommendation appears less of a concern than excessive deference to management recommendations.

Lastly, it is important to bear in mind that the largest mutual fund groups – Vanguard, Fidelity, and American – vote substantially independently of ISS and each accounts for about 20% the aggregate assets in the sample and roughly 11% of the total long-term assets under

management by all mutual funds.⁵⁹ Thus, at least as far as mutual funds are concerned, these three major fund families control at least as many votes, and probably more, than those that strictly follow ISS.

This being said, it is likely that ISS exercises substantial soft influence over shareholder voting. ISS is in the business of giving voting advice. ISS voting recommendations, and the reasons for these recommendations, are issued to a large subscriber base (which includes most institutional investors). ISS tries, in formulating its voting policies, to incorporate its subscribers' preferences.⁶⁰ Thus, while ISS's control over voting decisions through funds that have a strong tendency to follow ISS recommendations is limited, a much larger pool of assets is voted in a manner substantially correlated with the ISS recommendation. This correlation is due either to these funds basing their votes to some extent, depending on the reasons for the recommendation and on other fund concerns, on the ISS recommendation or to ISS taking into account the concerns of institutional investors in arriving at their recommendation (so if funds dislike directors who are absent from board meetings then the ISS recommendation will take attendance into account and fund votes will correlate with the ISS recommendation as a result).⁶¹

As Table 3 shows, funds managing 36% of the sample assets have a probability of voting withhold, conditional on ISS recommending a withhold vote, of between 40% to 70%.⁶² (Only 2% of the sample assets both fall in this category and follow ISS 97.5% or more of the time.) Put differently, for about one-third of the mutual fund assets under management, if ISS makes a

⁵⁹ Data on mutual fund asset holdings as of March 31, 2007, provided by Mr. Erin H. Short, Senior Research Associate, Statistical Research, Investment Company Institute.

⁶⁰ See ISS, Policy Formulation and Application, <http://www.issgovernance.com/policy/process> (last visited Aug. 15, 2011) (explaining that annual survey of institutional investors is part of the process by which ISS formulates its voting policies).

⁶¹ See Choi et al., *supra* note __ (Emory) at 882-85 (discussing possible explanations for correlation between ISS recommendations and voting outcomes).

⁶² We compute the 36% from Table 3 as follows: funds managing 27% of the sample assets have a probability of voting withhold, conditional on ISS recommending a withhold vote, of between 40% and 50%; funds managing 4% of the sample assets have a probability of voting withhold, conditional on ISS recommending a withhold vote, of between 50% and 60%; and funds managing 5% of the sample assets have a probability of voting withhold, conditional on ISS recommending a withhold vote, of between 60% and 70%.

withhold recommendation, there is a roughly 50% probability that the fund will vote withhold. Between the smaller asset pool that toes the ISS line in most of the cases, and the much larger asset pool that votes in accordance with ISS in about half of the cases, an ISS withhold recommendation is associated with a significant change in the vote.

Table 3: Fund Withhold Votes and ISS Withhold Recommendations

Percentile	Fund WH conditional on ISS WH		Fund WH that follow ISS WH	
	Assets (\$ millions)	Percentage of Assets	Assets (\$millions)	Percentage of Assets
0 - .1	1,127,831	0.45	994,182	0.39
.1 - .2	183,526	0.07	262,599	0.10
.2 - .3	14,764	0.01	594,636	0.24
.3 - .4	73,100	0.03	11,970	0.00
.4 - .5	678,171	0.27	71,012	0.03
.5 - .6	95,714	0.04	4,079	0.00
.6 - .7	137,591	0.05	99,363	0.04
.7 - .8	5,374	0.00	35,278	0.01
.8 - .9	122,681	0.05	156,480	0.06
.9 - 1	80,664	0.03	177,764	0.07
No Withholds	na	na	112,052	0.04

"Fund WH conditional on ISS WH" is defined as the probability of a withhold vote for a specific director by a fund conditional on ISS giving a withhold recommendation for the director. "Fund WH that follow ISS WH" is defined as the number of withhold votes by a specific fund when ISS also gives a withhold recommendation divided by the total number of withhold votes by the specific fund. Percentile categories tabulate data from those funds that fit into the specific category (e.g., "0 - .1" reports on those funds that have a "Fund WH conditional on ISS WH" between 0% and 10% and those funds that have a "Fund WH that follow ISS WH" between 0.0 and 0.1).

The significance of this influence is enhanced by two further factors. First, a substantial percentage of the sample asset pool never, or virtually never, votes withhold. This pool consists of mutual funds that employ the shortcut of following board recommendations and shareholders that are affiliated with the board or the issuer.⁶³ In addition, we conjecture that withhold votes

⁶³ Insiders, who are unlikely ever to vote withhold, own substantial percentages of some issuers. For example, founders David Filo and Jerry Yang own more than 3% of Yahoo (Yahoo 2010 Proxy Statement at 36). Similarly founder and CEO Warren Buffet and director Bill Gates (through the Bill and Melinda Gates Foundation) own more than 3% of Berkshire Hathaway. See Berkshire Hathaway 2010 Proxy Statement, dated March 11, 2010 at 8.

are rare among some groups of individual shareholders and private pension plans.⁶⁴ Second, although there are many withhold votes on director nominees on which ISS recommended a “for” vote (see Table 3, last two right columns),⁶⁵ these votes are not highly correlated. As a result, if ISS does not issue a withhold recommendation, a director is very unlikely to receive a high withhold vote. An ISS withhold recommendation thus represents a focal point for fund voting. Although funds may not vote in accordance with a particular ISS withhold recommendation, it is more likely that many multiple funds will vote withhold on a particular nominee for which ISS recommended withhold than on a particular nominee for which ISS recommended a for vote.

As measure of, and evidence for, this focal point effect, we calculated the correlation in voting among ISS and the dominant clusters of the 19 large fund families in our sample. The correlation was significant and positive between ISS and 17 of the clusters. In comparison the average number of significant correlations between any one cluster and the 18 other clusters was 11.4. The average correlation between ISS and the dominant clusters of only large fund families was also significantly higher than the average correlation among the clusters.⁶⁶

Finally, considering the facts that institutional investors account for 60% of the stock holdings in the years for which we collected vote data, that ISS recommendations are unlikely to

⁶⁴ We note that during the time period of our study, brokers retained discretionary voting authority in uncontested director elections. As a result, many retail shares were voted in favor of management. See Kara Scannell & Dan Fitzpatrick, SEC Plans to End Broker Vote Rule, in *Win for Activists*, WALL ST. J., Apr. 24, 2009 at C1 (“Since 1937, the brokers have been able to vote their clients’ shares, and have typically voted in favor of standing managements and boards.”).

⁶⁵ For example, as reported in Table 3, 39% of sample assets have a “Fund WH that follow ISS WH” of between 0.0 to 0.1 indicating that most of the fund withhold votes occur when ISS gives a for recommendation for this category of funds.

⁶⁶ This being said, four clusters had a higher average correlation with the other clusters than with ISS – the families were Alliance Bernstein, Hartford, Morgan Stanley and T. Rowe Price – and one family (T. Rowe Price) had a number of significant correlations equivalent to ISS. These four clusters generally voted similarly, but only two of them were characterized as following an ISS shortcut. The other two families -- T. Rowe Price and Morgan Stanley – had a similar overall withhold rate as did ISS, but declined to follow ISS withhold recommendations in, respectively, 16% and 37% of all cases and their withhold votes that did not follow ISS accounted for, respectively, 12% and 22% of their total withhold votes.

affect votes by individual investors,⁶⁷ and that part of the correspondence between ISS withhold recommendations and fund withhold votes can be explained by the fact that ISS and funds arrive at the same decision by independently considering the same factors, these data on ISS's influence on mutual funds are consistent with our prior estimate that ISS's affects 6-10% of the total vote. Our data is also consistent with our prior conclusion that ISS acts as information agent, the recommendations of which are followed selectively based on the rationale given and the fund's independent evaluation of the rationale.⁶⁸

Perhaps the biggest shortcoming of ISS then is that it does not explain its recommendations to vote for the company nominees and thus does not permit its clients to evaluate these for vote evaluations independently. This failure may account for the focal point nature of an ISS withhold recommendations. Absent an ISS withhold recommendation, even when there are legitimate grounds for a "withhold" vote, the failure of ISS to explain its analysis means many shareholders will lack relevant information, making it difficult to galvanize a high number of withhold votes.

IV. Fund Independence

Many mutual fund management companies are affiliated with other units, such as commercial and investment banks or insurance companies ("affiliated funds"). These fund managers may have a special interest in not alienating management of their portfolio companies – by voting against board nominees to the board – in order to maintain good business relations or generate new business for their affiliates. A mutual fund complex may pursue various strategies in this regard. The complex might vote differently with respect to portfolio companies that are

⁶⁷ See Choi et al., *supra* note __ (Emory) at 901 (explaining that, because ISS recommendations are provided to institutional investors on a subscription basis, they are unlikely to affect votes by retail investors substantially).

⁶⁸ See *id.*

clients or prospective clients.⁶⁹ This strategy, however, entails substantial disadvantages.

Employees of the adviser would need to generate lists of current and prospective clients, and those lists would need to be incorporated into the fund's voting decisions. Furthermore, the effect of client considerations on voting decisions, if it becomes known, is likely to generate adverse publicity and potential liability.

An easier and safer strategy would be for a fund to employ a general voting pattern for all portfolio companies that does not endanger business relations. Specifically, the fund could establish a policy of avoiding withhold votes for all portfolio companies, regardless of whether the company is an existing or prospective client. Alternatively, the fund could seek cover by presumptively following ISS recommendations. Even though ISS will occasionally recommend a withhold vote, the fund could deflect responsibility for its vote by pointing to the fund's general policy of following ISS on the principle of "don't take it personally, they made me do it."

Although the fund would remain responsible for its policy of following ISS, it is presumably far easier to defend such a general policy to a client than an internal fund decision to vote against a director nominee to the client's board.

As we have seen, many fund clusters do employ one of these strategies. In this part, we examine whether these strategies are more prevalent among affiliated funds than among independent funds. We first examine only dominant fund clusters. Dominant clusters are most likely to reflect the voting preferences and policies of centralized fund family management – the board or the fund sponsor – whereas funds in non-dominant clusters may be more influenced by the concerns of individual fund managers. We then consider all funds.

1. Dominant Clusters

⁶⁹ The SEC identified this as a potential concern when it adopted its rules requiring disclosure of mutual fund voting. See Disclosure of Proxy Voting Policies, *supra* note ____.

Of the 56 fund families in our sample, 28 are independent and 28 are affiliated. Table 4 shows the distribution of primary and secondary short-cut patterns for each group.

Table 4: Affiliated and Independent Funds (Dominant Clusters) – Use of Short-cuts

	Affiliated	Independent
Primary Follow Board	3	5
Secondary Follow Board	2	2
Primary Follow ISS	2	5
Secondary Follow ISS	6	2
No Short-cut	15	14

The data do not provide evidence that affiliated funds are more likely to adopt a strategy of following board recommendations than independent funds. In chi-squared tests, the difference in the proclivity to use the primary or secondary shortcut of following the board, compared to not using either short-cut, is insignificant (Pearson $\chi^2(2) = 0.5909$; $Pr = 0.744$). Moreover, the data do not support the notion that affiliated funds are more likely to adopt a strategy of following ISS recommendations than independent funds. In chi-square tests, the difference in the propensity to use the primary or secondary short-cut of following ISS, compared to not using either short-cut, is insignificant (Pearson $\chi^2(2) = 3.3101$ $Pr = 0.191$).

More generally, we examined the withhold rates of dominant fund clusters, both absolute and relative to the withhold recommendations issued by ISS (reported in Table 5). Dominant clusters in independent funds had a higher average and median withhold rate than dominant funds in affiliated clusters. The differences, however, are not statistically significant.

Table 5: Affiliated and Independent Funds (Dominant Clusters) – Withhold rates

	Absolute Withhold Rate	Relative Withhold Rate*
Average – Independent Funds	0.066	1.134
Average – Non-Independent Funds	0.047	0.778
Median – Independent Funds	0.040	0.885
Median – Non-Independent Funds	0.036	0.592

* Relative withhold rate is the fund’s withhold rate relative to the ISS withhold recommendation rate for the set of directors on which the fund voted. A relative withhold rate greater than 1, for example, indicates that the fund withholds more frequently than ISS recommends withhold.

Deleted: votes

Finally, we looked at the five dominant clusters than had withhold rates at least twice as high as ISS. Two of them were at affiliated funds, three at independent funds. Thus, even with respect to clusters with very high withhold rates, there is no major difference in voting behavior between affiliated and independent funds.

2. All Funds

We now consider all funds within a fund family. We start with an analysis of all fund clusters similar to the one we performed for dominant clusters. As Table 6 shows, clusters in affiliated fund complexes are more likely to be independent and less likely to follow any short-cuts than clusters in independent complexes. In chi-squared tests, however, the difference between following either set of short-cuts and not following them is not statistically significant. Moreover, we caution that dominant and non-dominant fund clusters can be of highly unequal size, relative to the total assets of a fund complex. Thus, any analysis that gives equal weight to each cluster can be misleading. To take an extreme example, the dominant cluster in the Target fund complex accounts for 63% of the aggregate assets in target and is coded as employing no short-cut, while a non-dominant cluster in the Target family accounted for only 1% of the assets and is coded as employing a secondary follow ISS short-cut.

Table 6: Affiliated and Independent Funds (All Clusters) – Use of Short-cuts

	Affiliated	Independent
Primary Follow Board	7	6
Secondary Follow Board	3	2
Primary Follow ISS	4	6
Secondary Follow ISS	15	11
No Short-cut	50	23
Total Clusters	79	48

As a final step, we analyze fund complex withhold rates. To do this, we calculated the fund complex absolute withhold rate as the average withhold rate of all clusters within a fund weighted by the percentage of assets in each cluster. The average (median) withhold rate in independent fund complexes was 0.067 (0.046) and the average (median) withhold rate in affiliated fund complexes was 0.051 (0.041). Compared to the rates for dominant clusters, the withhold rates for affiliated fund complexes are somewhat larger, but still below those for independent complexes. The difference remained statistically insignificant.

On the whole, therefore, we do not find significant evidence that affiliated fund complexes adopt voting policies designed to maintain good business relationship with portfolio companies for other business units, either by adopting general policies of following board recommendations or by adopting a policy of following ISS recommendation and just avoiding responsibility for individual voting decisions.

V. How the Largest Funds Vote

Three mutual fund complexes – Vanguard, Fidelity, and American funds – tower over all other funds in terms of assets under management. Each of them had more than \$1 trillion under management during 2005-06. Together, these three families account for 34% of aggregate mutual fund assets during our sample period. Moreover, all Vanguard and American funds vote fully or virtually fully in lockstep, as does the dominant cluster of Fidelity funds (the non-index

funds), which accounts for 90% of Fidelity's aggregate assets. By comparison, the next largest fund family, Franklin Templeton, is roughly one-third the size of these three, and its dominant cluster accounts for only 72% of its assets.

The factors that influence the voting decisions of these three fund complexes are thus of particular interest. To see how specific director and company attributes related to the probability of a withhold vote, we tabulated the fund complexes' votes for directors along several attributes and calculated whether the probability that a director with a certain attribute (e.g. a CEO) received a withhold vote from a certain fund complex (e.g. Vanguard) was significantly higher or lower than the average probability of a withhold vote for that specific complex. Tables A1 to A3 in the Appendix report the summary statistics. For a definition of the attributes, see the Appendix. In prior research, we have shown that most of the attributes affect the voting recommendations of proxy advisors and the shareholder vote.⁷⁰

We divided the attributes into several categories and subcategories as follows: audit/disclosure related attributes (AuditMbr, Prior Restat, Prior SEC); compensation related attributes (CompMbr, Top5AbComp); board related attributes with the following subcategories: board effectiveness (Attendance, ManyBds, Age75); board composition (NomMbr), board independence (Empl_Dir, OutDirLink, Interlock) and board responsiveness (IP No -- shareholder proposal ignored); takeover related attributes (ClassBd, CumVote, Poison Pill, and Golden Parachute); performance related attributes (Top5AbRet and Bot5Abret); and uncategorized attributes (New Director, CEO, and ISS recommendation).⁷¹

We then ran logistic regressions for Vanguard, American, and the Fidelity non-index fund clusters using company-director-year level data (e.g., how the Vanguard funds voted for a specific director at a specific company in a particular year would form one data point in the

⁷⁰ See Choi et al., supra note __ (S. Cal.)

⁷¹ See the Appendix for definitions of the variables.

Vanguard fund cluster logistic model). The dependent variable in the models is the specific fund cluster's voting decision (either for = 1 or withhold = 0). In each logistic regression model, we included the above attributes and other factors as independent variables. Errors are clustered by company in the models.

A. Vanguard

Vanguard cast withhold votes for about 10% of the director candidates on which it voted. The summary statistics (see Appendix, Table A1) indicate that Vanguard was significantly more likely to withhold its vote from members of compensation or nominating committees and significantly less likely to withhold its vote from CEOs, other directors who are company employees, non-executive chairmen, and new directors. We caution, however, that these variables are correlated (e.g., the CEO is ordinarily not a member of the compensation committee) and the causal relationship accounting for the vote is thus unclear.

This being said, it is notable that, of 1,435 Vanguard withhold votes, 1,087 (over 75%) were cast against members of a company's compensation committee even though such directors account for only 39% of the nominee pool. This strongly suggests that a large fraction of Vanguard's withhold votes are driven by compensation-related matters for which Vanguard holds members of the compensation committee responsible. Consistent with this focus on compensation, Vanguard is also significantly more likely to cast a withhold vote against board members on companies that paid abnormally high compensation, and even more likely to cast a withhold vote against the members of the compensation committees of such companies.

Other factors that are associated with a Vanguard withhold vote in the univariate analysis are failure to attend at least 75% of the board meetings, being an outside linked director, and bottom 5% abnormal return. By contrast, membership on many boards, ignoring shareholder proposals, and having a poison pill or a golden parachute are associated with a *reduction* in the probability of a Vanguard withhold vote.

Although we classified Vanguard as voting independently, Vanguard's votes are significantly correlated with the ISS recommendations. Vanguard followed 40% of the ISS withhold recommendations, but voted withhold for only 9% of the directors for which ISS recommended a "for" vote. We should note that this degree of correlation does not mean that Vanguard follows an ISS short-cut. Rather, Vanguard rejected a majority (60%) of ISS's withhold recommendations and 76% of Vanguard's withhold votes were cast on directors for which ISS recommended a "for" vote. Vanguard thus does not follow ISS blindly, or even usually, but instead regularly departs from ISS recommendations. We believe that this pattern results from one of two underlying mechanisms. First, Vanguard may independently use some of the same underlying factors in making its voting decisions that ISS uses in its recommendations. Second, Vanguard may consider the ISS recommendations, and the reasons ISS provides for them, selectively and as one of several factors in its voting decision.

The company-director-year vote logistic regressions using the Vanguard vote as the dependent variable (see Appendix, Table A4) confirm the importance of compensation-related factors for Vanguard's voting decisions. We first consider model (1), which includes the variables from the univariate analysis of Appendix Table A1 as independent variables, except that it does not include the ISS recommendation as an independent variable. The variables for CompMbr and Top5AbComp are significant, at the 1% and 5% levels respectively, and of large absolute magnitude. At the mean level for the other variables, membership on the compensation committee and high compensation are estimated to increase the probability of a Vanguard withhold vote by, respectively, 16% and 6%. The large coefficient estimate for membership on a compensation committee is of particular interest since there is nothing per se problematic about such membership. (In contrast, other variables, such as non-attendance at board meetings, prior restatement, and even an ISS withhold recommendation, are per se indicators of some problem.) The large coefficient estimate thus indicates not merely that compensation-related factors are

important for Vanguard, but also that a large percentage of compensation committees do not live up to Vanguard's standards.

Other variables that are associated with an increased probability of a withhold vote are OutDirLink, Empl_Dir, and Attendance, each at the 1% level. At the mean level for the other variables, these factors are estimated to increase the probability of a Vanguard withhold vote by, respectively, 22%, 11% and 62%. Being a member of the nominating or audit committee is also associated with an increased probability of a withhold vote, but the later are significant only at the 10% level, and they have only a marginal quantitative effect on the probability of a Vanguard withhold vote. In contrast, New Director, Chairman Only, and Top5AbRet significantly reduce the probability of a withhold vote (at the 1%, 5% and 10% levels, respectively). Of the takeover related attributes, having a classified board increases, but having a poison pill reduces the probability of a withhold vote.

In model (2), the added variable for the ISS recommendation is highly significant, reflecting, as noted, the correlation between Vanguard votes and ISS recommendations. The quantitative impact, while important, is not overwhelming. At the mean level for the other variables, an ISS withhold recommendation increases the probability of a Vanguard withhold vote by 14% (compared to 51% for failure to attend at least 75% of the board meetings, 16% for being an outside linked director, and 15% for being a member on the compensation committee (all from model (2)). The inclusion of the ISS variable has little effect on the significance of the other variables except that Top5AbRet, with was borderline significant in model (1), is now borderline insignificant and IP No is now associated with a significant (at the 5% level) *reduction* in the probability of a withhold vote.⁷²

⁷² In our assessment, this does not signify that Vanguard prefers directors who ignore shareholder proposals that receive majority support, but rather reflects Vanguard's selective approach to ISS withhold recommendations. As we have shown elsewhere, IP No is a powerful factor in explaining ISS withhold recommendations. However, the summary statistics and the regression in model (1) indicate that IP No does not explain Vanguard withhold votes.

B. American Funds

The American Funds group was classified as voting according to board recommendations. American Funds cast withhold votes in a mere 16 of over 4,000 director elections, a withhold rate of 0.4%. (See Appendix, Table A2) The very rare withhold votes by American are substantially attributable to withholding votes from directors on companies that restated their financial statements. As shown in the summary statistics, over half (9 of the 16) the withhold votes relate to directors at such companies, even though these directors account for only 10% of the director nominees on which American cast a vote. Given that the company restated its financials, being a member of the audit committee did not further increase the probability of a withhold vote.

The summary statistics point to no other factor that seems to explain withhold votes by the American fund complex. Notably, neither Attendance and OutDirLink – which we have shown elsewhere are important factors in explaining withhold recommendations by ISS and shareholder voting overall and which, as shown above, have a significant impact on Vanguard's voting – appears to affect the voting of the American fund complex. In addition, in the univariate analysis, the ISS recommendation has no impact on the vote by American funds.

In the company-director-year vote logistic regressions using the American vote as the dependent variable (see Appendix, Table A5), as one would expect, the coefficient for Prior Restat is highly significant and, in absolute magnitude, dwarfs all of the other coefficient estimates. While the interaction variable Prior Restat x AuditMbr is significant and negative, the variable for AuditMbr is of similar magnitude and significantly positive. This means that, given a restatement, being a member of the audit committee does not further increase the

Likewise, while Vanguard may heed ISS withhold recommendations (or independently arrive at the same conclusions as ISS) with respect to some reasons for withhold votes, Vanguard does not follow ISS withhold recommendations that are based on the company's ignoring a shareholder proposal. In model (2), this is reflected in the significant negative coefficient for the ISS recommendation and the significant positive coefficient (or similar magnitude) for IP No, which balance each other out for ISS withhold recommendations issued because the director ignored a shareholder proposal.

probability of a withhold vote. In addition, being a new director increases the probability of a withhold vote. Albeit statistically significant, in absolute terms, the effects of being a member of the audit committee and being a new director are trivial. When we add the variable for the ISS recommendation (in Table A5 model (2)), the significance levels of these other variables does not change and the ISS variable itself is insignificant.

C. Fidelity

Fidelity funds vote in two separate clusters. Most Fidelity funds, other than its index funds, vote in lockstep with each other and form what we term the “dominant Fidelity cluster”. These funds represent 90% of the equity assets under management by the Fidelity group. The second cluster consists of the Fidelity index funds, which also vote in lockstep with each other, but differently from the dominant Fidelity cluster. This cluster comprises the remaining 10% of equity assets under management by the Fidelity group.

Our analysis here concerns only the dominant Fidelity cluster (the non-index funds). Turning to the voting of that cluster, Fidelity’s withhold rate was about 3%. In the summary statistics (Appendix, Table A3), factors associated with an increased probability of a withhold vote included audit-related factors (Prior Restat, Prior SEC, as well as the interaction variables Prior Restat x AuditMbr and Prior SEC x AuditMbr), Empl_Dir, Age75, as well as three takeover-related factors (ClassBd, Poison Pill, and Golden Parachute). Curiously, our variable for low abnormal return (Bot5AbRet) was associated with a reduced probability of a withhold vote. Fidelity funds were also slightly more likely to withhold their vote on directors when ISS recommended a withhold vote (4.4%) than when ISS recommended a “for” vote (2.9%).

As to the company-director-year vote logistic regression using the Fidelity non-index fund vote as the dependent variable, our explanatory variables do a relatively poor job in explaining Fidelity’s voting behavior (see Appendix, Table A6). This is reflected, for one, in the low pseudo r-squared of the logistic regressions (0.082 and 0.084 depending on the model). R-

squared is a variable that measures the fraction of the variation in the dependent variable – i.e. Fidelity voting decision – that is explained by the independent variables. For comparison, the respective pseudo r-squares are 0.243 and 0.270 for Vanguard and 0.277 and 0.282 for American. This suggests that Fidelity’s voting decisions, to a substantially greater extent than Vanguard’s and American’s, are affected by factors not accounted for in our analysis.

Taking a closer look at the independent variables, in model (1) (without the ISS variable) prior restatements increase the probability of a Fidelity withhold vote for members of the audit committee, as does being an employee director. In addition, one takeover related factor (Golden Parachute) increases the probability of a withhold vote. As for American fund, Attendance, IP No and OutDirLink are not significant. Model (2) yields equivalent results, and the ISS recommendation is insignificant.

D. Comparison of Large Fund Voting with Overall Shareholder Voting and ISS Recommendations

In our earlier articles, we examined the factors that determine the overall percentage for vote directors received in election as well as the factors that determine the ISS voting recommendations. Our analysis here of the voting by the Vanguard, American and Fidelity fund complexes enables us to compare the voting behavior of these large institutional investors with each other as well as with the votes of shareholders overall and the ISS recommendations.

Table 7 below summarizes how these factors affect the voting decision. Two results stand out. First, the three large mutual fund families differ from each other not only in the overall withhold rate, but also in the factors that determine withhold votes. Second, the factors that affect the voting outcome correspond more closely to the factors that affect the ISS recommendation than to the factors that affect the voting decisions by Vanguard, American and Fidelity. This is true even if we control for the ISS recommendation itself in examining the

factors that affect the voting outcome. The latter finding supports the conclusion in our earlier article that ISS is more in tune with voter sentiments at large than other market participants.⁷³

Looking at the three large fund families individually, the factors that affect Vanguard's vote are very similar to the factors that affect ISS recommendations and (to the lesser extent) the factors that affect voting decisions. The major, and very important, difference is the dramatic effect of compensation-related matters on Vanguard's vote. For Vanguard, being a member of the compensation committee raises the probability of a withhold vote by 16%, from roughly 5% to 21%. For ISS, the corresponding increase is a mere 2%. Importantly, 39% of all nominees for which Vanguard cast a vote were members of a compensation committee. Thus, the material increase in withhold vote probability with such membership has a much larger effect on Vanguard's vote than the larger increase in withhold vote probability for the few (0.7% of director pool) directors who missed more than 25% of the board meetings.

A second notable difference relates to the fact that Vanguard does not hold it against board members if they ignore a shareholder proposal that received majority support. In contrast, ignoring a shareholder proposal vastly increases the probability of a ISS withhold recommendation (by 42%) and is also associated with an approximately 2% decline in the for vote *beyond* the average effect of an ISS recommendation. This factor, however, affects only about 1% of the director nominees.

The American fund complex differs from both ISS and voters at large (and, for that matter, from Vanguard and Fidelity) in its very strong presumption of voting for all company nominees. Even in the rare cases where the American funds withhold their vote from a nominee, the factor we identify is distinctive in that the presence of a prior restatement neither affects the ISS recommendation nor the voting outcome at large.

⁷³ See, e.g., Choi, et al., *supra* note __ (Emory) at 906.

As to Fidelity, the most notable observation is the dog that did not bark. Factors related to compensation, board governance, and performance – important to ISS, Vanguard, and voters at large – have little or no impact on Fidelity. For that matter, none of the factors we identify have a large effect on Fidelity’s voting. This being said, it is possible that other factors, which we did not take into account in our analysis, affect both Fidelity’s voting decision and the overall voting outcome.

Table 7: Comparison of Factors Affecting Votes and ISS Recommendation

Factor	Category	ISS Rec.	Aggregate Vote Outcome Exc. ISS	Aggregate Vote Outcome Inc. ISS	Vanguard Vote Exc. ISS	Vanguard Vote Inc. ISS	American Vote Exc. ISS	American Vote Inc. ISS	Fidelity Vote Exc. ISS	Fidelity Vote Inc. ISS
CEO		_***	_***	_***						
New Dir.		+***	+***	+***	+**	+**				
Audit	Audit		_***	_***	_*	_*				
PriorRestat	Audit						_***	_***		
PriorSEC	Audit		_***	_***						
CompMbr	Comp.	_***	_***	_***	_***	_***				
Top5Ab Comp	Comp.	_*			_**	_**				
Attendance	Board – Effect.	_***	_***	_***	_***	_***				
ManyBds	Board – Effect.	_***	_***	_***						
Age75	Board – Effect.		_***	_***						
NomMbr	Board – Comp.	_***	_***	_***	_***					
Empl_Dir	Board – Indep.	_***	_***	_***	_***	_***			_**	_**
OutDirLink	Board – Indep.	_***	_***	_***	_***	_***		+**		
Chairman Only		+**			+**	+**				
IP No	Board – Respon.	_***	_***	_***		+**				
ClassBd	Takeover	_**	_***	_***	_**	_**				
Poison Pill	Takeover				+**	+**				
CumVote	Takeover	_*								
Golden Parachute	Takeover	+***							_*	_*
Top5AbRet	Performance		+**	+**	+*					
Bot5AbRet	Performance		_**	_***						

* , ** , *** signify statistical significance of the factor at the 10%, 5% and 1% levels.

"ISS Rec." is from a model with the ISS recommendation (For or WH) as the dependent variable. See Choi et al., supra (USC Paper). "Aggregate Vote Outcome Exc. ISS" is from a model with the log odds of the total for vote as a fraction of all votes cast as the dependent variable without VoteISS (the ISS recommendation) as an independent variable. "Aggregate Vote Outcome Inc. ISS" is the same as "Aggregate Vote Outcome Exc. ISS" but including VoteISS as an independent variable. See Choi et al., supra (Emory). The Vanguard, American, and Fidelity regressions use the respective fund's vote as the dependent variable and are reported in Appendix Tables A4 to A6.

+, - signify direction. ++, -- signify a larger quantitative impact. In the non-outcome regressions, we considered an impact large if it was statistically significant and our quantitative estimate at the median for other factors was either (i) at least 10% or (ii) at least 5% and the factor was present for at least 10% of the

nominees. Statistically significant factors with a quantitative impact of less than 1% are omitted. In the outcome regressions, we treated an impact as large if it was associated with a coefficient of greater than 1.

VI. What Explains Large Withhold Votes

The voting decisions of the three large mutual funds, together with other data we have collected, also enable us to analyze the factors associated with directors who received high withhold votes. For purposes of this examination, we define a high withhold vote as a withhold vote of 30% or more of the votes cast.⁷⁴ During 2005 and 2006, 276 directors in our sample received high withhold votes.

Table 8, Panel A below provides information about directors who received a high withhold vote. For the entire set of directors in our sample, the probability of getting a high withhold vote is 2%. For directors who received an ISS withhold recommendation, the probability of a high withhold vote jumps to 30% and these directors account for 95% of the set of directors who received a high withhold vote. Correspondingly, for directors who did not receive an ISS withhold recommendation, the probability of a high withhold vote drops to 0.1%.

Among directors with an ISS withhold recommendation, directors who have one of the following four characteristics are particularly prone to receiving a high withhold vote: first, directors for whom Fidelity cast a withhold vote (79% probability of receiving a high withhold vote); second, directors who did not attend at least 75% of the board meetings (60% probability); third, directors at companies that ignored a shareholder resolution that received majority support (35% probability); and fourth, directors for whom Vanguard cast a withhold vote and who are also outside linked directors (40% probability).

If these four groups are combined, they account for 48% of the directors who received a high withhold vote and directors who fall in any one of the groups have a 49% probability of receiving a high withhold vote. In comparison, a director who received an ISS withhold

⁷⁴ Cf. Huckleby, *supra* note __ at 1 (defining as “high” a withhold vote of 20% or more); Diane Del Guercio, Laura Seery & Tracie Woidtke, Do boards pay attention when institutional investor activists “just vote no”?, 90 J. Fin. 84 (2008) (describing withhold votes of more than 20% as “substantial”).

recommendation but is *not* in one of these groups only has a 21% probability of receiving a high withhold vote. This figure is still substantially above the respective probability for directors who did not receive an ISS withhold recommendation, but it is less than half of the respective probability for directors who are in one of the four groups. Furthermore, outside of the four groups, a Vanguard withhold vote did not make much difference; directors who received an ISS withhold recommendation and for whom Vanguard cast a withhold vote (but who are not in one of the four groups) had a 18% probability of receiving a high withhold vote, slightly less than the respective directors for whom Vanguard did not cast a withhold vote.

If we define high withhold more narrowly, as directors receiving more than 40% or more than 50% withhold votes, the pattern becomes even stronger (reported in Table 8 Panels B and C). Directors who receive an ISS withhold recommend and who are in one of the four groups account, respectively, for 56% and 81% of the pool of directors who received in excess of 40% or in excess of 50% withhold votes. For directors who are within one of the groups, the probability of receiving a 40% or more or 50% or more withhold vote is, respectively, 19% and 5%. For directors who received an ISS withhold recommendation but who are not in one of the groups, the probability of receiving such a high withhold vote is significantly lower (7% and 0.5%, respectively).

Our analysis thus suggests that the four factors we have identified, in conjunction with ISS recommendations, have substantial explanatory power in predicting whether a director receives a high withhold vote at multiple thresholds. An adverse ISS recommendation that is not combined with one of the factors increases the probability of receiving a high withhold vote by a factor of 5 to 10. The presence of one of the factors on top of the ISS recommendation increases the probability of a high withhold vote by a further factor of 2.5 to 10. The higher the threshold

of what amounts to a high withhold vote, the less important the ISS recommendation is on its own and the more important is the additional presence of one of the factors. This finding reinforces the suggestion in our prior research that ISS's recommendations are influential for their informational value, particularly to the extent that ISS identifies problems that shareholders independently view as important.

Table 8: Panel A: Over 30% Withhold Votes

	(1) All Direc- tors	(2) ISS WH	(3) ISS WH + Fidelity WH	(4) ISS WH + Atten- dance	(5) ISS WH + Shareholder Resolution	(6) ISS + Vangd. WH + Outside Linked Director	(3) – (6) Combined
Pool	13159	887	29	40	52	174	281
High WH Vote	276	262	23	24	18	69	134
High WH Vote/Pool	0.02	0.30	0.79	0.60	0.35	0.40	0.48
High WH Vote/Total High WH Vote	1.00	0.95	0.08	0.09	0.06	0.25	0.49

Table 8: Panel B: Over 40% Withhold Votes

	(1) All Direc- tors	(2) ISS WH	(3) ISS WH + Fidelity WH	(4) ISS WH + Atten- dance	(5) ISS WH + Shareholder Resolution	(6) ISS + Vangd. WH + Outside Linked Director	(3) – (6) Combined
Pool	13159	887	29	40	52	174	281
High WH Vote	97	97	10	16	4	24	54
High WH Vote/Pool	0.01	0.11	0.34	0.40	0.08	0.14	0.19
High WH Vote/Total High WH Vote	1.00	1.00	0.10	0.16	0.04	0.25	0.56

Table 8: Panel C: Over 50% Withhold Votes

	(1) All Direc- tors	(2) ISS WH	(3) ISS WH + Fidelity	(4) ISS WH + Atten-	(5) ISS WH + Shareholder	(6) ISS + Vangd.	(3) – (6) Combined
--	---------------------------	------------------	-----------------------------	---------------------------	--------------------------------	------------------------	-----------------------

	tors		WH	dance	Resolution	WH + Outside Linked Director	
Pool	13159	887	29	40	52	174	281
High WH Vote	16	16	2	4	0	7	13
High WH Vote/Pool	0.001	0.02	0.07	0.10	0.00	0.04	0.05
High WH Vote/Total High WH Vote	1.00	1.00	0.13	0.25	0.00	0.44	0.81

It is notable that the combination of an ISS withhold recommendation and a Fidelity withhold vote (which is associated with a 79% probability of a high withhold vote) is particularly problematic for directors -- much more so than the combination of an ISS withhold recommendation and a Vanguard withhold vote (which is associated with only a 36% probability of a high withhold vote). As we have discussed earlier, the factors in our model do not explain Fidelity's voting behavior well and the correlation between Fidelity's voting and ISS recommendation is much lower than the equivalent correlation between Vanguard and ISS. Thus, ironically, while Fidelity's voting appears largely independent from ISS, in the relatively infrequent instances where Fidelity and ISS agree, the director is in trouble.

Less surprisingly, lack of regular attendance at board meetings is highly significant in explaining high withhold votes. For the >40% and >50% thresholds (Panels B and C), the combination of an ISS withhold recommendation and lack of regular attendance was the best predictor we found for directors receiving a high withhold vote. Specifically, this combination raised the background probability of receiving a majority withhold vote by a factor of 100. Moreover, lack of regular attendance (unlike a Fidelity withhold vote) is also a strong predictor of getting an ISS withhold recommendation.

The significance of attendance is somewhat expected given prior findings by us and others that attendance is an important factors in explaining the vote outcome and Vanguard’s voting (in either case, with and without controlling for the ISS recommendation), as well as the voting recommendations of other proxy advisors.⁷⁵ Lack of attendance is also relatively easy for shareholders to observe directly because SEC rules require companies to identify specifically, in the proxy statement itself, any director who did not attend at least 75% of the board meetings.⁷⁶

The two other factors – ignoring a shareholder resolution (IP No) and the combination of a Vanguard withhold vote and being an outside linked director (OutDirLink) – are less strongly associated with a high withhold vote. In our prior studies, we found that ignoring a shareholder resolution is a strong predictor of an ISS withhold recommendation (in fact, a stronger predictor than lack of attendance)⁷⁷ and a significant factor in explaining the vote outcome (though less important than attendance, being an employee director, or being an outside linked director).⁷⁸ Shareholders cannot directly observe whether directors have ignored a prior shareholder resolution by reviewing the current proxy statement, however, as the SEC does not require disclosure equivalent to that mandated for a director’s lack of attendance. We find that ignoring a prior shareholder resolution is also less of a factor in explaining voting recommendations of other proxy advisors and not relevant at all in explaining the votes of Vanguard or Fidelity.⁷⁹ Still, given its effect on ISS and given the substantial difference in the probability of a high withhold hold associated with a “regular” ISS withhold recommendation and an ISS withhold recommendation based on a failure to implement a shareholder issue proposal that received

⁷⁵ See Choi et al, supra note __, and Cai et al., supra note __.

⁷⁶ SEC rules require issuers to disclose the name of each director who attended fewer than 75% of the meetings of the board and of committees on which he or she sat. STANDARD INSTRUCTIONS FOR FILING FORMS UNDER SECURITIES ACT OF 1933, SECURITIES EXCHANGE ACT OF 1934 AND ENERGY POLICY AND CONSERVATION ACT OF 1975—Regulation S-K, 17 C.F.R. § 229.407 (b).

⁷⁷ See Choi et al, supra note __ and supra, Part V.

⁷⁸ See Choi et al, supra note __.

⁷⁹ See Choi et al, supra note __.

majority shareholder support in the prior year, directors take a big chance in ignoring shareholder resolutions.

The combination of an ISS withhold recommendation, a Vanguard withhold vote and being an outside linked director is associated with a much higher probability of a high withhold vote than merely receiving an adverse ISS recommendation and a Vanguard withhold vote or merely receiving an adverse ISS recommendation and being an outside linked director. We suspect that this is due to the presence of some additional factors that make being an outside linked director more objectionable than are both correlated with a high overall withhold vote and with a Vanguard withhold vote.

Conclusion

This paper has tried to address an increasingly important question: what factors explain the voting of mutual funds? We find that the voting of funds in the same fund family tends to be centralized, more so in small than in large fund families. We also find that a significant minority of funds have adopted voting strategies to follow presumptively the voting recommendations of either management or ISS, again with these strategies more common in smaller than larger fund families. We find, however, no evidence that fund families affiliated with banks or insurance companies vote differently from independent funds. Thus, our research does not support the claim that fund voting is influenced by business ties between fund affiliates and portfolio companies.

Looking more closely at ISS, we find evidence that its influence is, to a substantial degree, due to funds that use its recommendations as an input into a further, independent analysis, rather than to funds that follow ISS recommendations without much independent thought. This evidence should alleviate concerns about excessive power of ISS. We further find

substantial heterogeneity in mutual fund voting. Specifically, the three largest fund families – Vanguard, Fidelity, and American funds, exhibit significantly different voting patterns from each other, both in terms of their overall proclivity to cast withhold votes and in terms of the factors explaining these votes, as well as in relation to ISS recommendations. This suggests an avenue for further research to study whether it would be desirable to require large institutional investors to release their voting intentions in advance of the annual meeting to provide additional information to other market participants.

Finally, we identify four factors that, in conjunction with ISS recommendations, explain which directors are likely to receive withhold votes in excess of 30%. These findings are of special import for companies and directors who want to avoid such embarrassingly high withhold votes.

Our research documents the use by funds of their increasing voting power, and we are hopeful that, as funds become more experienced and sophisticated participants in the election process, they will consider improving their attempts to hold directors accountable beyond the efforts that we find here.⁸⁰ Although some scholars have questioned the ability of institutional investors to improve issuer performance through shareholder activism,⁸¹ it is nonetheless true that the most promising mechanism for increasing board accountability is intelligent voting by those shareholders with a meaningful economic interest in the results of those votes.

⁸⁰ See, e.g., Yonca Ertimur, Fabrizio Ferri & David A. Maber, Reputation Penalties for Poor Monitoring of Executive Pay: Evidence from Option Backdating, *___ J. Fin. Econ. ___* (forthcoming 2011), avail. at <http://ssrn.com/abstract=1638216> (finding that, although investors withheld votes from directors at firms involved in options backdating scandals, they did not withhold votes from those same directors at firms not involved in the scandals).

⁸¹ See, e.g., Roberta Romano, Less is More: Making Institutional Investor Activism a Valuable Mechanism of Corporate Governance, 18 *Yale J. Reg.* 174 (2001) (finding that institutional activism through shareholder proposals does not improve, and in some cases damages, firm performance).

APPENDIX
Variable Definitions

Variable	Definition
CEO	Indicator variable equal to 1 if the director is the CEO of the company in question and 0 otherwise.
New Director	Indicator variable equal to 1 if the director has been on the board for less than 2 years and 0 otherwise.
AuditMbr	Indicator variable equal to 1 if the director is a member of the audit committee and 0 otherwise.
Prior Restat	Indicator variable equal to 1 if news relating to a financial restatement was first made public within 2 years prior to the meeting date (either in a SEC filing or through a public press release) and 0 otherwise.
Prior SEC	Indicator variable equal to 1 if news relating to a SEC investigation or enforcement action was first made public within 2 years prior to the meeting date (either in a SEC filing or through a public press release) and 0 otherwise.
CompMbr	Indicator variable equal to 1 if the director is a member of the compensation committee and 0 otherwise.
Top5AbComp	Indicator variable equal to 1 if the total excess compensation for the CEO for the company in question is in the top 5% of the sample and 0 otherwise. We define total excess CEO compensation as the difference between the total CEO compensation for the year prior to the meeting date (as provided by the Compustat Executive Compensation database) minus the expected total CEO compensation. We calculate the expected total CEO compensation by (1) estimating an OLS model for Total CEO compensation = a + b1market_capitalization + b2One_Year_Abnormal_Holding_Period_Return + b3Year_2006 + e. (2) Using the predicted Total CEO compensation based on this model as the expected Total CEO compensation.
Attendance	Indicator Variable equal to 1 if director attended less than 75% of the meetings and 0 otherwise (as tracked by IRRRC for the year prior to the annual meeting date).
ManyBds	Indicator variable equal to 1 if the director is a member of at least three other "major" company boards (as followed by IRRRC for the year prior to the annual meeting date) and 0 otherwise.
Age75	Indicator variable equal to 1 if the director is 75 years or older and 0 otherwise.
NomMbr	Indicator variable equal to 1 if the director is a member of the nominating committee and 0 otherwise.
Empl_Dir	Indicator variable equal to 1 if the director is an employee of the company in question (but not the CEO) and 0 otherwise.

OutDirLink	Indicator variable equal to 1 if the director is an outside director of the company in question with affiliated links with the company and 0 otherwise. IRRC treats as linked a director: “who is a former employee; is an employee of or is a service provider, supplier, customer; is a recipient of charitable funds; is considered an Interlocking or designated director; or is a family member of a director or executive.” See “Definitions for RiskMetrics’ Directors Dataset” available at http://wrds.wharton.upenn.edu/ds/riskmetrics/dir_doc.shtml .
TotDirSH	The percentage of the votes in the company in question held by all board members.
Interlock	Indicator Variable equal to 1 if director met the IRRC criteria for an Interlocking director in the year prior to the annual meeting date and 0 otherwise. IRRC defines an Interlocking directorship as follows: “whereby a director and executive of the company sits on a board of another company that has an executive and director who also sit[s] on the original company’s board.” See “Definitions for RiskMetrics’ Directors Dataset” available at http://wrds.wharton.upenn.edu/ds/riskmetrics/dir_doc.shtml .
Chairman Only	Indicator variable equal to 1 if the director is the chairman of the board of the company in question but not an employee and 0 otherwise.
IP No	Indicator variable equal to 1 if the company in question faced a proxy issue proposal that received a majority for vote in the year prior to the director vote in question and failed to implement the recommendations of the proxy issue proposal and 0 otherwise.
ClassBd	Indicator variable equal to 1 if the director sits on a classified board for the company in question (as measured by IRRC for the year prior to the annual meeting date) and 0 otherwise.
Poison Pill	Indicator variable equal to 1 if a poison pill exists for the company in question (as measured by IRRC for the year prior to the annual meeting date) and 0 otherwise.
CumVote	Indicator variable equal to 1 if the company in question uses cumulative voting to elect directors (as measured by IRRC for the year prior to the annual meeting date) and 0 otherwise
Golden Parachute	Indicator variable equal to 1 if the company in question uses golden parachute agreements (as measured by IRRC for the year prior to the annual meeting date) and 0 otherwise.
Top5AbRet	Indicator variable equal to 1 if the abnormal return for the three-year period prior to the annual meeting date for the company in question is in the top 5% of the sample and 0 otherwise. The abnormal return is defined as the difference between the raw three-year holding period return for the company in question and the three-year holding period return for the CRSP value weighted market index.

Bot5AbRet	Indicator variable equal to 1 if the abnormal return for the three-year period prior to the annual meeting date for the company in question is in the bottom 5% of the sample and 0 otherwise. The abnormal return is defined as the difference between the raw three-year holding period return for the company in question and the three-year holding period return for the CRSP value weighted market index.
Sdret	Standard deviation of returns for the company in question for the one-year period prior to the annual meeting date.
ln(Mktcap)	Log of the market capitalization (in \$ millions) of the company in question.
InstHold	Percentage of shares of the company in question held by institutional investors.
Year06	Indicator variable equal to 1 if the director recommendation is for 2006 and 0 otherwise (for 2005).
VoteISS	Indicator variable equal to 1 if ISS recommends a Withhold vote for the director in question and 0 otherwise.

Appendix Table A1: Vanguard Vote Summary Statistics

	Total Votes	=0 N	FOR	WH	ForVote	=1 N	FOR	WH	ForVote	Chi-Squared p-value
All	13,427					13,427	11992	1435	89.3%	
ISS REC (1=WH)	13,424	12,566	11,476	1,090	91.3%	858	513	345	59.8%	0.000
CEO	13,483	12,057	10,649	1,408	88.3%	1,426	1,393	33	97.7%	0.000
New Director	13,483	11,332	10,012	1,320	88.4%	2,151	2,030	121	94.4%	0.000
AuditMbr	13,483	8,098	7,228	870	89.3%	5,385	4,814	571	89.4%	0.797
Prior Restat	13,483	11,861	10,596	1,265	89.3%	1,622	1,446	176	89.1%	0.820
Prior SEC	13,483	12,562	11,212	1,350	89.3%	921	830	91	90.1%	0.412
Prior Restat x AuditMbr	13,483	12,832	11,459	1,373	89.3%	651	583	68	89.6%	0.838
Prior SEC x AuditMbr	13,483	13,147	11,742	1,405	89.3%	336	300	36	89.3%	0.987
CompMbr	13,483	8,267	7,913	354	95.7%	5,216	4,129	1,087	79.2%	0.000
Top5AbComp	12,885	12,248	11,004	1,244	89.8%	637	525	112	82.4%	0.000
Top5AbComp x CompMbr	12,885	12,656	11,377	1,279	89.9%	229	152	77	66.4%	0.000
Attendance	13,443	13,353	11,971	1,382	89.7%	90	31	59	34.4%	0.000
ManyBds	12,864	11,619	10,403	1,216	89.5%	1,245	1,120	125	90.0%	0.641
ManyBds x CEO	12,864	12,813	11,473	1,340	89.5%	51	50	1	98.0%	0.047
Age75	13,483	13,043	11,674	1,369	89.5%	440	368	72	83.6%	0.000
NomMbr	13,483	8,161	7,472	689	91.6%	5,322	4,570	752	85.9%	0.000
Empl_Dir	13,483	12,642	11,257	1,385	89.0%	841	785	56	93.3%	0.000
OutDirLink	13,483	12,066	10,951	1,115	90.8%	1,417	1,091	326	77.0%	0.000
Interlock	13,483	13,451	12,014	1,437	89.3%	32	28	4	87.5%	0.740
Chairman Only	13,483	13,184	11,761	1,423	89.2%	299	281	18	94.0%	0.008
IP No	13,483	13,377	11,940	1,437	89.3%	106	102	4	96.2%	0.021
ClassBd	13,290	8,558	7,654	904	89.4%	4,732	4,220	512	89.2%	0.646
Poison Pill	13,290	6,362	5,650	712	88.8%	6,928	6,224	704	89.8%	0.055
CumVote	13,290	11,794	10,522	1,272	89.2%	1,496	1,352	144	90.4%	0.171
Golden Parachute	13,290	3,324	2,874	450	86.5%	9,966	9,000	966	90.3%	0.000
Top5AbRet	13,478	12,781	11,424	1,357	89.4%	697	613	84	87.9%	0.233
Bot5AbRet	13,478	12,868	11,507	1,361	89.4%	610	530	80	86.9%	0.047
Top5AbRet x CEO	13,478	13,393	11,953	1,440	89.2%	85	84	1	98.8%	0.004
Bot5AbRet x CEO	13,478	13,406	11,967	1,439	89.3%	72	70	2	97.2%	0.029

For each variable =0 is for director who do not meet the criteria and =1 if for directors who do meet the criteria. (For example, CEO = 0 represents directors who are not CEOs). "FOR" is the number of directors in the =0 or =1 subgroup that received a for vote from Vanguard. "WH" is the number of directors in the =0 or =1 subgroup that received a withhold vote from Vanguard. ForVote is the for vote as a percentage of all for and withhold votes cast for directors in the =0 and

=1 subgroups of directors by Vanguard funds for each criteria. The chi-squared p-value is from a chi-squared test of the difference in the relative frequencies of for and withhold votes for directors who are =0 and =1 for the specific criteria in the table.

Appendix Table A2: American Vote Summary Statistics

	Total Votes	=0 N	FOR	WH	ForVote	=1 N	FOR	WH	ForVote	Chi-Squared p-value
All	4,324					4,324	4,308	16	99.6%	
ISS REC (1=WH)	4,327	4,092	4,077	15	99.6%	235	234	1	99.6%	0.885
CEO	4,351	3,942	3,928	14	99.6%	409	407	2	99.5%	0.670
New Director	4,351	3,706	3,694	12	99.7%	645	641	4	99.4%	0.251
AuditMbr	4,351	2,687	2,675	12	99.6%	1,664	1,660	4	99.8%	0.275
Prior Restat	4,351	3,923	3,916	7	99.8%	428	419	9	97.9%	0.000
Prior SEC	4,351	3,917	3,901	16	99.6%	434	434	0	100.0%	0.182
Prior Restat x AuditMbr	4,351	4,183	4,170	13	99.7%	168	165	3	98.2%	0.002
Prior SEC x AuditMbr	4,351	4,190	4,174	16	99.6%	161	161	0	100.0%	0.432
CompMbr	4,351	2,807	2,796	11	99.6%	1,544	1,539	5	99.7%	0.723
Top5AbComp	4,249	3,961	3,945	16	99.6%	288	288	0	100.0%	0.280
Top5AbComp x CompMbr	4,249	4,150	4,134	16	99.6%	99	99	0	100.0%	0.536
Attendance	4,347	4,320	4,304	16	99.6%	27	27	0	100.0%	0.751
ManyBds	4,189	3,634	3,620	14	99.6%	555	553	2	99.6%	0.929
ManyBds x CEO	4,189	4,171	4,155	16	99.6%	18	18	0	100.0%	0.792
Age75	4,351	4,244	4,228	16	99.6%	107	107	0	100.0%	0.525
NomMbr	4,351	2,693	2,682	11	99.6%	1,658	1,653	5	99.7%	0.572
Empl_Dir	4,351	4,100	4,085	15	99.6%	251	250	1	99.6%	0.934
OutDirLink	4,351	3,881	3,866	15	99.6%	470	469	1	99.8%	0.557
Interlock	4,351	4,340	4,324	16	99.6%	11	11	0	100.0%	0.840
Chairman Only	4,351	4,259	4,243	16	99.6%	92	92	0	100.0%	0.556
IP No	4,351	4,320	4,304	16	99.6%	31	31	0	100.0%	0.734
ClassBd	4,336	3,074	3,058	16	99.5%	1,262	1,262	0	100.0%	0.010
Poison Pill	4,336	2,441	2,425	16	99.3%	1,895	1,895	0	100.0%	0.000
CumVote	4,336	3,862	3,846	16	99.6%	474	474	0	100.0%	0.160
Golden Parachute	4,336	1,147	1,140	7	99.4%	3,189	3,180	9	99.7%	0.116
Top5AbRet	4,346	4,254	4,238	16	99.6%	92	92	0	100.0%	0.556
Bot5AbRet	4,346	4,209	4,193	16	99.6%	137	137	0	100.0%	0.470
Top5AbRet x CEO	4,346	4,335	4,319	16	99.6%	11	11	0	100.0%	0.840
Bot5AbRet x CEO	4,346	4,331	4,315	16	99.6%	15	15	0	100.0%	0.814

For each variable =0 is for director who do not meet the criteria and =1 if for directors who do meet the criteria. (For example, CEO = 0 represents directors who are not CEOs). "FOR" is the number of directors in the =0 or =1 subgroup that received a for vote from American. "WH" is the number of directors in the =0 or =1 subgroup that received a withhold vote from American. ForVote is the for vote as a percentage of all for and withhold votes cast for directors in the =0 and =1 subgroups of directors by American funds for each criteria. The chi-squared p-value is from a chi-squared test of the difference in the relative frequencies of for and withhold votes for directors who are =0 and =1 for the specific criteria in the table.

Appendix Table A3: Fidelity Non Index Fund Vote Summary Statistics

	Total Votes	=0 N	FOR	WH	ForVote	=1 N	FOR	WH	ForVote	Chi-Squared p-value
All	10,112					10,112	9,814	298	97.1%	
ISS REC (1=WH)	10,112	9,453	9,181	272	97.1%	659	630	29	95.6%	0.026
CEO	10,150	9,088	8,815	273	97.0%	1,062	1,034	28	97.4%	0.504
New Director	10,150	8,555	8,308	247	97.1%	1,595	1,541	54	96.6%	0.281
AuditMbr	10,150	6,149	5,960	189	96.9%	4,001	3,889	112	97.2%	0.426
Prior Restat	10,150	8,990	8,758	232	97.4%	1,160	1,091	69	94.1%	0.000
Prior SEC	10,150	9,315	9,052	263	97.2%	835	797	38	95.4%	0.005
Prior Restat x AuditMbr	10,150	9,687	9,415	272	97.2%	463	434	29	93.7%	0.000
Prior SEC x AuditMbr	10,150	9,844	9,557	287	97.1%	306	292	14	95.4%	0.092
CompMbr	10,150	6,283	6,086	197	96.9%	3,867	3,763	104	97.3%	0.198
Top5AbComp	9,803	9,196	8,922	274	97.0%	607	586	21	96.5%	0.503
Top5AbComp x CompMbr	9,803	9,587	9,299	288	97.0%	216	209	7	96.8%	0.840
Attendance	10,131	10,054	9,756	298	97.0%	77	74	3	96.1%	0.631
ManyBds	9,699	8,675	8,417	258	97.0%	1,024	998	26	97.5%	0.435
ManyBds x CEO	9,699	9,659	9,375	284	97.1%	40	40	0	100.0%	0.271
Age75	10,150	9,859	9,572	287	97.1%	291	277	14	95.2%	0.060
NomMbr	10,150	6,157	5,970	187	97.0%	3,993	3,879	114	97.1%	0.597
Empl_Dir	10,150	9,532	9,257	275	97.1%	618	592	26	95.8%	0.060
OutDirLink	10,150	9,081	8,815	266	97.1%	1,069	1,034	35	96.7%	0.529
Interlock	10,150	10,130	9,830	300	97.0%	20	19	1	95.0%	0.591
Chairman Only	10,150	9,923	9,626	297	97.0%	227	223	4	98.2%	0.280
IP No	10,150	10,063	9,767	296	97.1%	87	82	5	94.3%	0.125
ClassBd	10,024	6,612	6,439	173	97.4%	3,412	3,287	125	96.3%	0.003
Poison Pill	10,024	4,792	4,690	102	97.9%	5,232	5,036	196	96.3%	0.000
CumVote	10,024	9,053	8,776	277	96.9%	971	950	21	97.8%	0.118
Golden Parachute	10,024	2,530	2,496	34	98.7%	7,494	7,230	264	96.5%	0.000
Top5AbRet	10,145	9,533	9,252	281	97.1%	612	592	20	96.7%	0.651
Bot5AbRet	10,145	9,746	9,448	298	96.9%	399	396	3	99.2%	0.008
Top5AbRet x CEO	10,145	10,071	9,772	299	97.0%	74	72	2	97.3%	0.893
Bot5AbRet x CEO	10,145	10,102	9,801	301	97.0%	43	43	0	100.0%	0.251

For each variable =0 is for director who do not meet the criteria and =1 if for directors who do meet the criteria. (For example, CEO = 0 represents directors who are not CEOs). "FOR" is the number of directors in the =0 or =1 subgroup that received a for vote from the Fidelity Non Index funds. "WH" is the number of directors in the =0 or =1 subgroup that received a withhold vote from the Fidelity Non Index funds. ForVote is the for vote as a percentage of all for and withhold votes cast for directors in the =0 and =1 subgroups of directors by Fidelity Non Index funds for each criteria. The chi-squared p-value is from a chi-squared test of the difference in the relative frequencies of for and withhold votes for directors who are =0 and =1 for the specific criteria in the table.

Appendix Table A4: Vanguard

	Model (1)	Model (2)
CEO	-0.0484 (-0.20) [-0.0023]	0.0965 (0.41) [0.0042]
New Director	0.485** (3.85) [0.0196]	0.410** (3.23) [0.0162]
AuditMbr	-0.185+ (-1.78) [-0.0088]	-0.189+ (-1.76) [-0.0086]
Prior Restat	0.116 (0.57) [0.0052]	0.116 (0.54) [0.0050]
Prior SEC	-0.0153 (-0.05) [-0.0007]	-0.0144 (-0.05) [-0.0006]
Prior Restat x AuditMbr	-0.103 (-0.41) [-0.0050]	-0.0926 (-0.36) [-0.0043]
Prior SEC x AuditMbr	-0.410 (-0.99) [-0.0229]	-0.451 (-1.13) [-0.0246]
CompMbr	-2.353** (-19.08) [-0.1594]	-2.330** (-18.98) [-0.1512]
Top5AbComp	-0.899* (-2.42) [-0.0612]	-0.876** (-2.67) [-0.0567]
Top5AbComp x CompMbr	-0.288 (-0.60) [-0.0153]	-0.265 (-0.58) [-0.0133]
Attendance	-3.667** (-10.93) [-0.6163]	-3.247** (-9.02) [-0.5084]
ManyBds	0.0981 (0.71) [0.0044]	0.234 (1.54) [0.0096]
ManyBds x CEO	-0.508 (-0.49) [-0.0299]	-0.841 (-0.81) [-0.0554]

Age75	-0.0648 (-0.36) [-0.0031]	-0.0561 (-0.32) [-0.0026]
NomMbr	-0.241** (-2.71) [-0.0115]	-0.210* (-2.28) [-0.0096]
Empl_Dir	-1.331** (-5.16) [-0.1075]	-1.030** (-4.34) [-0.0707]
OutDirLink	-2.163** (-15.16) [-0.2241]	-1.825** (-12.24) [-0.1624]
TotDirSH	-1.487** (-2.68) [-0.0695]	-1.319* (-2.49) [-0.0591]
Interlock	0.837 (1.62) [0.0273]	0.592 (1.20) [0.0205]
Chairman Only	0.749* (2.36) [0.0257]	0.675* (2.14) [0.0228]
IP No	1.161 (1.31) [0.0335]	1.982* (2.22) [0.0409]
ClassBd	-0.304* (-2.38) [-0.0148]	-0.293* (-2.19) [-0.0137]
Poison Pill	0.249* (1.98) [0.0117]	0.274* (2.09) [0.0124]
CumVote	0.251 (1.32) [0.0107]	0.319 (1.60) [0.0128]
Golden Parachute	0.182 (1.30) [0.0089]	0.134 (0.92) [0.0062]
Top5AbRet	0.420+ (1.75) [0.0166]	0.389 (1.55) [0.0149]
Bot5AbRet	0.301 (1.38) [0.0124]	0.313 (1.28) [0.0124]

Top5AbRet x CEO	0.191 (0.21) [0.0082]	0.317 (0.38) [0.0123]
Bot5AbRet x CEO	-0.184 (-0.24) [-0.0093]	-0.127 (-0.15) [-0.0060]
Sdret	-49.50** (-6.42) [-2.3143]	-44.41** (-5.47) [-1.9892]
Inmktcap	0.140** (2.87) [0.0066]	0.146** (2.87) [0.0065]
InstHold	-1.167* (-2.14) [-0.0546]	-1.210* (-2.12) [-0.0542]
Year06	0.560** (5.07) [0.0266]	0.556** (4.83) [0.0253]
VoteISS		-1.624** (-8.98) [-0.1419]
Constant	4.446** (5.92)	4.375** (5.60)
<i>N</i>	12163	12123
pseudo <i>R</i> ²	0.243	0.270

t statistics in parentheses; * $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$. Dependent variable Vote = 1 if the fund voted "for" and 0 if the fund voted "withhold" for the director in question. Errors are clustered by company. Marginal effects on the probability of a for vote for each coefficient are in brackets. For indicator variables, the marginal effect on the for vote probability is for a change from 0 to 1.

Appendix Table A5: American

	Model (1)	Model (2)
CEO	-0.240 (-0.96) [-0.0009]	-0.242 (-0.98) [-0.0008]
New Director	-0.873** (-3.61) [-0.0039]	-0.881** (-3.89) [-0.0039]
AuditMbr	1.198** (4.11) [0.0035]	1.154** (5.00) [0.0032]
Prior Restat	-2.791* (-2.17) [-0.0387]	-2.913* (-2.15) [-0.0421]
Prior Restat x AuditMbr	-1.515** (-3.64) [-0.0109]	-1.450** (-4.56) [-0.0097]
CompMbr	0.00409 (0.01) [0.0000]	-0.00198 (-0.00) [0.0000]
ManyBds	-0.127 (-0.30) [-0.0004]	-0.115 (-0.23) [-0.0004]
NomMbr	0.152 (0.31) [0.0005]	0.224 (0.41) [0.0007]
Empl_Dir	-0.429 (-1.07) [-0.0017]	-0.471 (-1.15) [-0.0018]
OutDirLink	0.524 (0.40) [0.0014]	0.875 (1.02) [0.0020]
Sdret	-43.84 (-1.26) [-0.1406]	-51.80 (-1.42) [-0.1607]
Inmktcap	-0.546* (-1.96) [-0.0018]	-0.540+ (-1.90) [-0.0017]
InstHold	-9.279 (-1.49) [-0.0298]	-9.079 (-1.49) [-0.0282]
Year06	1.190	1.084

	(0.85)	(0.81)
	[0.0045]	[0.0039]
VoteISS		-1.476
		(-1.32)
		[-0.0099]
Constant	16.24**	16.33**
	(2.81)	(2.84)
<hr/>		
<i>N</i>	1233	1224
pseudo <i>R</i> ²	0.277	0.282

z statistics in parentheses; **p* < 0.10, ***p* < 0.05, ****p* < 0.01. Dependent variable Vote = 1 if the fund voted "for" and 0 if the fund voted "withhold" for the director in question. Errors are clustered by company. Marginal effects on the probability of a for vote for each coefficient are in brackets. For indicator variables, the marginal effect on the for vote probability is for a change from 0 to 1. Note that Prior SEC, Top5AbComp, Attendance, ManyBds x CEO, Age75, Interlock, Chairman Only, IP No, ClassBd, Poison Pill, CumVote, Top5Abret, Bot5Abret = 1 all predicted Vote = 1 (for vote) perfectly and were dropped from the models (along with the corresponding observations). Prior SEC x AuditMbr, Top5AbComp x CompMbr, Top5Abret x CEO, and Bot5Abret x CEO were dropped due to collinearity with other independent variables.

Appendix Table A6: Fidelity Non-Index Funds

	Model (1)	Model (2)
CEO	0.0872 (0.36) [0.002]	0.0981 (0.40) [0.0019]
New Director	-0.0578 (-0.30) [-0.0012]	-0.0785 (-0.41) [-0.0016]
AuditMbr	0.168 (1.08) [0.0033]	0.166 (1.07) [0.0033]
Prior Restat	-0.701 (-1.63) [-0.0187]	-0.687 (-1.57) [-0.0182]
Prior SEC	-0.652 (-1.43) [-0.0174]	-0.663 (-1.43) [-0.0178]
Prior Restat x AuditMbr	-0.348* (-2.12) [-0.0082]	-0.338* (-2.03) [-0.0080]
Prior SEC x AuditMbr	-0.109 (-0.70) [-0.0023]	-0.128 (-0.80) [-0.0027]
CompMbr	0.146 (1.01) [0.0029]	0.159 (1.10) [0.0032]
Top5AbComp	-0.294 (-0.45) [-0.0067]	-0.284 (-0.43) [-0.0065]
Top5AbComp x CompMbr	-0.0740 (-0.50) [-0.0016]	-0.0655 (-0.42) [-0.0014]
Attendance	-0.328 (-0.44) [-0.0078]	-0.193 (-0.25) [-0.0043]
ManyBds	0.00560 (0.03) [0.0001]	0.0227 (0.11) [0.0005]
Age75	-0.647 (-1.53) [-0.0178]	-0.640 (-1.50) [-0.0175]

NomMbr	-0.0223 (-0.18) [-0.0005]	-0.00925 (-0.07) [-0.0002]
Empl_Dir	-0.664* (-2.42) [-0.0180]	-0.633* (-2.27) [-0.0169]
OutDirLink	0.0610 (0.28) [0.0012]	0.135 (0.57) [0.0026]
TotDirSH	-0.816 (-0.87) [-0.0165]	-0.814 (-0.87) [-0.0165]
Interlock	-0.820 (-0.79) [-0.0251]	-0.886 (-0.85) [-0.0279]
Chairman Only	0.845 (1.63) [0.0119]	0.816 (1.56) [0.0116]
IP No	-0.750 (-0.71) [-0.0220]	-0.549 (-0.54) [-0.0145]
ClassBd	-0.272 (-0.72) [-0.0058]	-0.267 (-0.71) [-0.0056]
Poison Pill	-0.437 (-1.12) [-0.0088]	-0.442 (-1.12) [-0.0089]
CumVote	0.394 (0.58) [0.0069]	0.403 (0.59) [0.0070]
Golden Parachute	-1.331* (-2.46) [-0.0208]	-1.332* (-2.47) [-0.0208]
Top5AbRet	-0.422 (-0.64) [-0.0103]	-0.400 (-0.60) [-0.0096]
Bot5AbRet	1.606 (1.46) [0.0174]	1.634 (1.48) [0.0175]
Top5AbRet x CEO	0.200 (0.60) [0.0037]	0.220 (0.66) [0.0040]

Sdret	-22.84 (-0.96) [-0.4625]	-22.06 (-0.91) [-0.4462]
Inmktcap	0.121 (0.73) [0.0025]	0.119 (0.71) [0.0024]
InstHold	3.268* (2.02) [0.0662]	3.227* (1.97) [0.0653]
Year06	-0.791* (-2.25) [-0.0163]	-0.804* (-2.28) [-0.0166]
VoteISS		-0.429 (-1.08) [-0.0104]
Constant	3.121 (1.40)	3.159 (1.41)
<i>N</i>	9188	9158
pseudo <i>R</i> ²	0.082	0.084

t statistics in parentheses; * $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$. Dependent variable Vote = 1 if the fund voted "for" and 0 if the fund voted "withhold" for the director in question. Errors are clustered by company. Marginal effects on the probability of a for vote for each coefficient are in brackets. For indicator variables, the marginal effect on the for vote probability is for a change from 0 to 1. Note that ManyBds x CEO and Bot5Abret x CEO = 1 both predicted Vote = 1 (for vote) perfectly and were dropped from the models (along with the corresponding observations).