Understanding Uncontested Director Elections:
Determinants and Consequences

Yonca Ertimur
University of Colorado at Boulder
yonca.ertimur@colorado.edu

Fabrizio Ferri[*]
Columbia University
ff2270@columbia.edu

David Oesch
University of Zurich
david.oesch@business.uzh.ch

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Abstract:

We examine the determinants and consequences of voting outcomes at uncontested director elections. Exploiting a unique hand-collected dataset of the rationale behind proxy advisors' recommendations—the primary driver of voting outcomes—, we document the director and board characteristics that voting shareholders focus on (as well as those that they neglect), their evolution over time and their relative importance. We find that the percentage of votes withheld from directors increases with the severity of the underlying concerns, suggesting a certain degree of informed voting. Absent a negative recommendation, high votes withheld are extremely rare, highlighting the agenda setting role of proxy advisors, arguably a greater policy concern than their influence on shareholder votes. While high votes withheld rarely result in director turnover, our analyses show that firms often respond to an adverse vote by explicitly addressing the underlying concern (as proxied for by the rationale behind the recommendation). The rate of responsiveness increases in voting dissent and varies substantially with the rationale behind the vote. Overall, it appears that shareholders use their votes in uncontested director elections to get directors to address specific problems, rather than to vote them on or off the board, but they do so only on matters highlighted by the proxy advisors.

1. Introduction

Fueled by a series of corporate governance scandals and the recent financial crisis, shareholder activism has become increasingly prevalent over the past decade, with shareholder votes emerging as an important performance metric and control system (Fischer, Gramlich, Miller and White 2009).[1] One of the tools available to activist shareholders is withholding votes from nominees in uncontested director elections. In this study we exploit a unique hand-collected dataset that allows us to enhance our understanding of the factors driving shareholder votes in uncontested director elections, the effect of these votes on firms' actions and the impact of these actions on firm value.

We aim to contribute to prior research in three ways. First, while recommendations by the proxy advisory firm Institutional Shareholder Services (ISS) play a key role in determining voting outcomes (e.g., Cai, Garner and Walkling 2009; Ertimur, Ferri and Oesch 2013),[2] the question of what factors drive ISS recommendations and, thus, shareholder votes in uncontested director elections remains largely unanswered.[3] To fill this gap, we purchase the reports ISS releases to its clients and use the rationale behind negative ISS recommendations as a proxy for the rationale behind adverse shareholder votes. The frequency of these rationales over time and their association

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[1] Activism via shareholder votes at the annual meeting (on uncontested director elections, management proposals, shareholder proposals filed under Rule 14a-8) is a "low-cost" activism tool, in contrast to other forms of activism (e.g., hedge fund activism, proxy contests) where the power to influence the firm stems from the costly acquisition of a significant equity stake (Ferri 2012).

[2] Proxy advisors provide proxy voting services to institutional investors on a subscription basis, including voting recommendations and reports detailing the analysis underlying these recommendations. ISS, founded in 1985, is the dominant player in the market for proxy advisory services and develops its recommendations in consultation with its clients through an annual survey (see http://www.issgovernance.com/policy-gateway/policy-outreach/ for details). Glass Lewis (GL), founded in 2003, is the most influential competitor (Choi, Fisch and Kahan 2010).

[3] Cai et al. (2009) find that firm- and director-level characteristics have an economically negligible incremental impact on voting outcomes after controlling for the presence of a negative ISS recommendation (which is associated with 20% more votes withheld from a director). Relatedly, Cai et al. (2009) and Choi, Fisch and Kahan (2009) find that various director and firm attributes (observable to researchers) explain only a small portion of the variation in ISS recommendations. These findings highlight the challenge of trying to infer what factors truly affect shareholder votes without access to proxy advisors' reports.

with shareholder votes allows us to provide insights into the relative importance of the different factors shareholders focus on when voting in uncontested director elections.

Second, we focus on firms' responsiveness to shareholder votes and how it varies with the rationale behind the vote and with firm characteristics. While previous studies find that shareholder votes at director elections are associated with subsequent firm-level outcomes (e.g., higher CEO turnover, lower excess CEO pay, fewer and better acquisitions), as Fischer et al. (2009) note, it is not clear whether these outcomes are a response to the negative votes or to correlated omitted factors (e.g., behind-the-scene pressure from large institutional investors). Given the vast array of potential reasons underlying voting dissent, it is hard for researchers to causally link company actions to prior negative votes. For example, a mere association between a firm's decision to declassify the board and a prior negative vote on one or more of the director nominees cannot be interpreted as evidence of a firm's response to the vote. By combining our dataset on the rationale behind negative shareholder votes with hand-collected data on firms' governance changes explicitly made in response to the vote, we can link the firm's actions to the specific concerns underlying the negative vote. This approach speaks more directly to the causal effect of shareholder votes and allows us to identify the specific governance changes triggered by the votes. Continuing with the above example, a finding that firms are more likely to declassify the board subsequent to a negative shareholder vote driven by the classified board structure (but, importantly, not subsequent to a vote arising from other concerns—e.g., poor meeting attendance) would provide stronger support for inferring a causal influence of the vote on firm's behavior.[4] Hence, our approach allows us to provide more reliable and comprehensive evidence on the direct effect of uncontested director elections on firms' governance practices.

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[4] Conversely, a finding that the likelihood of declassifying the board is higher subsequent to a vote driven by unrelated factors (e.g. poor attendance by one director), but not subsequent to a vote related to the board classified structure, would suggest that there is no causal link between the shareholder vote and the firm's subsequent action.

Finally, while previous studies examine the association between votes withheld from directors and subsequent performance (e.g., Cai et al. 2009), we examine the performance consequences of firms' *responsiveness* to votes withheld, speaking to the broader question of the valuation effects of greater shareholder involvement in corporate governance (Cuñat, Gine and Guadalupe 2012).

We start our investigation by validating the rationale behind ISS recommendations as a proxy for the reason behind shareholders' votes. Using a sample of 23,844 director-firm-year observations for director elections held at S&P 500 firms over the 2003–2010 period from the ISS Voting Analytics database, we confirm that there is a statistically and economically significant association between shareholder votes and ISS recommendations in our setting. In particular, we show that a withhold recommendation from ISS is associated with approximately 20% more votes withheld from the director. Cases of high votes withheld absent a negative ISS recommendation are rare and most negative ISS recommendations result in high votes withheld; thus, there is almost a one-to-one mapping.[5] In contrast, the association between withhold recommendations from Glass Lewis (GL), ISS' main competitor, and shareholder votes is modest.

Having validated our proxy for the rationale behind shareholders' votes, for each director with an ISS withhold recommendation (1,673 cases; 7% of the sample), we obtain the underlying report, and read and categorize the rationale(s) for the recommendation. We group withhold recommendations into three broad categories, depending on whether the underlying concerns relate

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[5] Previous studies suggest three not mutually exclusive explanations for the positive association between ISS recommendations and shareholder votes (e.g. Choi et al. 2010). Namely, the association captures (i) the extent to which ISS recommendations coincide with independently formed shareholder preferences over governance, (ii) the percentage of uninformed votes cast by shareholders who mechanically follow ISS recommendations as a cost-effective way to fulfill their fiduciary duty to vote, and (iii) ISS's ability to synthesize and aggregate shareholder preferences. We discuss these explanations (and how our findings speak to their validity) in detail in Section 2.4. However, note that under all these explanations, the rationales underlying ISS recommendations are the *de facto* rationale behind shareholder votes.

to an individual director, every member of a committee or every board member, and each broad category into sub-categories to create a more granular description of the underlying rationale.

We then analyze the frequency of the reasons behind ISS withhold recommendations and their association with the voting outcome in order to provide insights in the relative importance of the factors shareholders focus on when voting in uncontested director elections. Individual-, committee- and board-level issues represent, respectively, 38.1%, 28.6% and 33.3% of the withhold recommendations. About two-thirds of the individual-level withhold recommendations stem from independence-related concerns, with the rest reflecting concerns with directors' busyness and attendance record. Almost all committee-level withhold recommendations pertain to executive pay (the largest driver of negative recommendations in the second half of the sample period). As for board-level withhold recommendations, 72.2% are due to lack of responsiveness to shareholder proposals receiving a majority vote (such as proposals to declassify the board) with most of the rest triggered by the adoption of a poison pill without shareholder approval.

We document substantial variation in votes withheld from directors conditional on the underlying reason. Consistent with the conjecture that the percentage of votes withheld will increase in the severity of the concerns underlying the vote, we find that votes withheld is higher when (i) the director receives a withhold for multiple reasons rather than a single reason (25.26% versus 20.47%), and (ii) the rationale behind the withhold is a board- or committee-level issue rather than an individual-level issue (25.48% and 19.73% relative to 16.44%). Shareholders also seem to take into account contextual factors other than the recommendation itself and its rationale when deciding how to cast their votes. In particular, shareholders are more likely to vote with ISS on a specific issue when they are already concerned with the governance structure of the firm, as proxied for by a high level of the entrenchment and the presence of excess CEO pay.

Next, we shift our attention to the economic consequences of shareholder votes in director elections, focusing in particular on firms' responses to the issues underlying negative votes (as proxied for by the rationale behind ISS recommendations). To do so, for each withhold recommendation in our sample we examine the ISS report issued ahead of the annual meeting and classify the firm as responsive if it addresses the specific problem highlighted the previous year.

Overall, the estimated rate of responsiveness ranges between 39.0% and 47.7% (depending on how we treat actions that only partially address the underlying issue). This is a fairly high figure considering that there are only a handful of cases where votes withheld exceed 50% and that it does not take into account actions firms take to avoid negative recommendations in the first place.[6] The rate of responsiveness varies significantly across individual-, committee- and board-level recommendations, as well as within each category. Notably, firms respond to 48.9% of the withhold recommendations arising from lack of responsiveness to majority-vote shareholder proposals. By definition, these are firms that ignored a shareholder proposal supported by a majority vote in the past and yet implement it in response to a (less than 50%) withhold vote, highlighting the greater effectiveness of a vote cast directly against directors themselves.

To mitigate the concern that the governance changes made subsequent to shareholder votes reflect a general trend or other economic determinants, we identify the most frequent concern behind the vote in each category (using the rationale behind ISS recommendation as a proxy) and examine responsiveness in a multivariate framework. In particular, we examine: (i) turnover on key committees (removing an affiliated director from these committees is the most common response to independence-related concerns, the most frequent individual-level issue), (ii) changes in abnormal CEO pay (compensation-related concerns are the most frequent issue in the

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[6] For comparison, over the 1997-2004 period, Ertimur, Ferri and Stubben (2010) report a rate of implementation of 31.1% for shareholder proposals supported by more than 50% of votes cast (with a peak of 40% in 2003-2004) versus only 3.2% for proposals receiving less than 50% of the majority vote.

committee-level category), and (iii) the likelihood of declassifying the board (most common issue in the lack of responsiveness sub-category of board-level recommendations). Across all three tests, we find a statistically and economically significant association between the specific governance change and the shareholder vote, but only when that governance issue is the reason behind the high votes withheld. For example, the likelihood of declassifying the board increases from 5.5% to 39.5% subsequent to a withhold recommendation for failure to implement majority-vote shareholder proposals to declassify the board. In contrast, and importantly, withhold recommendations due to other reasons do not have the same impact.

While establishing causality in our setting remains difficult, these analyses suggest that the documented governance changes are a direct response to the concerns behind the high votes withheld. This evidence also provides an explanation for the puzzle of the missing link between negative voting outcomes and subsequent director turnover (Cai et al. (2009), as well as this study) even when more than 50% of the votes are withheld from directors (so-called "zombie" directors—Bloomberg (2012)). Shareholders use their votes on uncontested director elections to get directors to address specific problems, rather than to vote them off the board, thereby explaining why most "zombie" directors keep their seats on corporate boards.

Finally, we compare the characteristics and subsequent performance of responsive and unresponsive firms. We find that firms are more likely to respond when shareholder pressure (proxied for by the percentage of votes withheld and the number of withhold recommendations) is higher and when performance is lower. However, there is no evidence of a difference in subsequent operating and stock performance between responsive and non-responsive firms, even in the most severe cases (e.g., board-level recommendations, high votes withheld). One explanation for these findings is that the items proxy advisors and voting shareholders focus on

have little effect on firm value, consistent with the claim that activists misdirect their efforts towards "symbolic" governance issues (Kahan and Rock 2014).

Our study contributes to several strands of literature. First, by providing the first comprehensive evidence on how firms respond to shareholder votes in uncontested director elections, we add to the limited research on boards' responsiveness to non-binding shareholder votes (Del Guercio, Seery and Woidtke 2008; Ferri and Sandino 2009; Ertimur et al. 2010, 2013; Cuñat et al. 2012). In doing so, we answer the call for more direct evidence on boards' actions, rather than the effect of those actions (Adams, Hermalin and Weisbach 2010).

Second, our findings contribute to the research on director elections (Del Guercio et al. 2008; Cai et al. 2009; Choi et al. 2009; Fischer et al. 2009) and, more generally, on boards of directors (e.g., DeFond, Hann and Hu 2005; Zhao and Chen 2008; Cai, Dhaliwal, Kim and Pan 2014; Kim, Mauldin and Patro, 2014). By examining the rationale behind ISS recommendations (the key driver of votes withheld) we identify the factors that voting shareholders de facto focus on (and the factors they neglect) in assessing directors' performance and qualifications, and in casting their votes. More importantly, we are able to establish a direct link between the concerns underlying a negative vote and the specific actions taken by the firm to address them, thereby shedding light on the effectiveness of uncontested director elections as a governance mechanism. Our evidence on shareholders' use of uncontested director elections to obtain specific governance changes rather than to vote directors on or off the board may also be of interest to regulators debating the desirability of proxy access (Becker, Bergstresser and Subramanian 2013).[7]

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[7] Proxy access refers to giving shareholders the right (under certain circumstances) to have their nominees included in the company's proxy statement alongside the board's nominees, without incurring the cost of a proxy contest. The Securities and Exchange Commission proposed mandatory proxy access in 2003, 2007 and 2010, but it was never implemented. For a history and details of the various proxy access proposals, see Kahan and Rock (2011).

Third, our study adds to a growing literature and may inform the policy debates on shareholder voting and the role of proxy advisors (Alexander, Chen, Seppi and Spatt 2010; Armstrong, Gow and Larcker 2013; Ertimur et al. 2013; Iliev and Lowry 2015; Larcker, McCall and Ormazabal 2013; Ferri and Maber 2013; SEC 2014). With respect to shareholder voting, our analysis of the performance implications of firms' responsiveness speaks to the merits of greater shareholder voice, which previous studies have examined mostly via event studies around governance reforms (Larcker, Ormazabal and Taylor 2011; Ferri and Maber 2013). With respect to the role of proxy advisors, on one hand, the variation in the sensitivity of shareholder votes to ISS withhold recommendations is inconsistent with the commonly held view (shared by the SEC) that the association between ISS recommendations and shareholder votes captures uninformed votes cast by investors who blindly follow ISS recommendations as a cost-effective way to fulfill their fiduciary duties.[8] On the other hand, our analysis highlights a subtle and more important aspect of proxy advisors' influence, their agenda-setting role. Cases of high votes withheld without a negative recommendation are basically non-existent, suggesting that shareholders are "active" only at the firms and on the topics singled out by proxy advisors, at the expense of other issues (e.g., directors' skill set, expertise and experience) for which proxy advisors have not (yet) developed voting guidelines but which are relevant to investors (Adams, Akyol and Verwijmeren 2013; Coles, Daniel and Naveen 2012; DeFond et al. 2005; Faleye, Hoitash and Hoitash 2011, 2013).

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[8] Our findings are consistent with Iliev and Lowry (2015), who examine mutual funds' votes and conclude that the influence of ISS is higher when the costs (benefits) of informed voting are higher (lower), and, thus the average association between ISS and shareholder votes is likely to significantly overstate the extent of uninformed voting. For example, Iliev and Lowry (2015) conclude that smaller mutual funds almost always follow ISS recommendations while larger funds (with more resources to do in-house research) deviate from ISS recommendations more often. We complement their findings by showing *when* shareholders choose to follow, or deviate from, ISS recommendations.

Finally, and more broadly, our study contributes to the literature on the effectiveness of various forms of shareholder activism (Brav, Jiang, Partnoy and Thomas 2008; Klein and Zur 2009; Bebchuk, Brav, and Jiang 2015).

2. What factors do shareholders focus on when voting on director elections?

2.1 Developing a proxy for the rationale behind shareholder votes

Institutional investors typically do not publicly disclose or comment upon the reason behind their votes. As a proxy for the reason behind shareholders' votes we use the rationale behind ISS recommendations. A necessary condition for the validity of this proxy is a statistically and economically significant association between votes and ISS recommendations. While prior literature suggests such an association exists (e.g., Cai et al. 2009; Ertimur et al. 2013), it is important to validate it and assess its extent in our setting. To do so, using the ISS Voting Analytics database we examine all uncontested director elections held at S&P 500 firms between 2003 and 2010, resulting in a sample of 23,844 director-firm-year-level observations (source: ISS Voting Analytics database).

Table 1 provides descriptive information on the percentage of votes withheld from directors (*Votes Withheld*).[9] As in prior studies (e.g., Cai et al. 2009), overall support for directors is quite high—the mean of votes withheld is 5%. However, when ISS issues a withhold recommendation (1,673 cases, 7.0% of the sample), the mean votes withheld is 24.70%, versus 3.6% when ISS issues a favorable recommendation; an increase of 21.1%.

Notably, 69.4% of the directors targeted by ISS receive votes withheld of more than 20%—a level typically viewed by boards as evidence of significant dissent (Del Guercio et al. 2008) and

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[9] We compute the percentage of votes withheld as the number of votes withheld from (cast against) the director scaled by the total number of votes cast for firms with a plurality (majority) voting standard. This is because in firms with a plurality (majority) voting standard shareholders are allowed to either vote for the director or *withhold* their vote (vote *against*) (Ertimur, Ferri and Oesch 2015).

there is no case of votes withheld greater than 50% without a negative ISS recommendation. In other words, there is not only a strong statistical association between high shareholder dissent and ISS recommendations, but also an almost one-to-one mapping: most negative ISS recommendations result in relatively high votes withheld, and rarely do high votes withheld occur absent a negative ISS recommendation, making the rationale behind ISS recommendations an appropriate proxy for the concerns behind shareholder votes.

In contrast, as in earlier studies (Choi et al. 2009; Ertimur et al. 2013), negative recommendations from the second most influential proxy advisor, Glass Lewis & Co (GL), are associated with an increase in votes withheld of only 8.0% (from 3.7% to 11.7%), likely due to GL's smaller client base (GAO 2007, Innisfree 2010).[10] As a result, only 17% of the directors targeted by GL receive votes withheld of more than 20%.

Next, we examine the association between proxy advisors' recommendations and votes withheld in a multivariate setting by estimating the following ordinary least squares regression:

$Votes\ Withheld = \alpha_0 + \alpha_1 ISS\ Withhold + \beta Control\ Variables\ + \varepsilon$ (1)

where *ISS Withhold* is an indicator equal to one if ISS issues a withhold for that director. Following prior studies (e.g., Cai et al. 2009), we control for a number of director and firm characteristics (see notes to Table 2 for details), and include year and industry fixed effects.

Table 2 reports the results excluding (Model 1) and including (Model 2) *ISS Withhold*. A withhold recommendation from ISS is associated with 20.6% more votes withheld from the director (similar to the univariate figures in Table 1) and results in a large increase in the explanatory power (adjusted R^2 of 64.1% in Model 2 versus 11.1% in Model 1). In contrast, the

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[10] As in other voting settings (e.g. say on pay) negative GL recommendations are more frequent (16.2% versus 7.0% for ISS), perhaps reflecting GL's strategy to cater to investors who tend to be more "activist" (Ertimur et al. 2013). Note that because GL was established in 2003, its recommendations are available only for the 2004 – 2010 period, explaining the smaller sample size in Table 1 (20,221 observations).

coefficient of *GL Withhold* (Model 3) indicates an association of only 4.6%, even less than the 8.0% suggested by Table 1.[11]

As in Cai et al. (2009), across the three models, many of control variables are statistically associated with the voting outcome (e.g. votes withheld are higher for linked directors, busy directors and directors failing to attend at least 75% of the meetings) but do not have an economically significant impact, with the exception of director attendance.[12, 13]

Based on the above results and to minimize the cost of hand-collecting these data, in the rest of the study we focus only on ISS recommendations at S&P 500 firms and use the rationale behind these recommendations as proxy for the rationale behind an adverse shareholder vote.[14] For the firm-years where at least one director receives an ISS withhold, we purchase the report ISS

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[11] Controlling for GL recommendations has a small impact on the coefficient of *ISS Withhold*, which only drops from 0.2201 (estimate from Model 2 for the subsample with GL observations, not tabulated) to 0.2077. We also examine a model where we replace the ISS and GL indicators with three indicators, denoting cases where only ISS, only GL, or both, issue a withhold. The coefficient of *Both ISS & GL Withhold* is positive and significant at 0.262 and is statistically larger than the sum of the coefficients on *Only ISS Withhold* (0.200) and *Only GL Withhold* (0.043), perhaps because some investors withhold their vote from a director only when both proxy advisors recommend doing so. But this difference is economically small (about 2% of the votes).

[12] Note that the voting penalty for directors who *Attend Less than 75% of Meetings* decreases from 11.18% in Model 1 to 5.26% in Model 2 because poor attendance is also a trigger for an ISS withhold (see Section 2.2), but does not disappear. This suggests that some shareholders vote against directors who fail to attend at least 75% of the meetings even in some cases where ISS concludes that that there is a valid reason. Illness is the most common, but not the only, valid reason. Consider the following example. "John R. Stafford was one meeting short of reaching the 75-percent attendance threshold. This was the first time during his 11-year tenure as a director that he attended fewer than 75 percent of meetings. Two of the meetings Mr. Stafford missed were due to re-scheduled or special meetings." (ISS Report 2005, Honeywell Inc.)

[13] We perform a number of additional analyses and robustness tests (untabulated). First, to control for firm-level fixed effects, following Cai et al. (2009) we use the difference between the percentage of votes withheld from the director and the mean percentage of votes withheld from all directors at that firm in the same year as the dependent variable. Our inferences are unchanged. Second, to alleviate concerns of potential multicollinearity between *ISS Withhold* and firm and director characteristics included in the regression, following Cai et al. (2009) we estimate Model 2 after replacing *ISS Withhold* with the residual from a logit regression of *ISS Withhold* on those firm and director characteristics (the pseudo R^2 is 9.5%). The coefficient of the residual, at 0.205, is positive and significant at the 1% level. Third, to examine whether shareholders' propensity to vote in line with ISS recommendations varies with the election standard (plurality versus majority voting; Ertimur et al. 2015), we interact the *ISS Withhold* indicator with an indicator for majority voting. The interaction term is not significant.

[14] We describe ISS voting policies on director elections in the next section and in Appendix 1. While a full comparison with GL voting policies is beyond the scope of our study, some of the key differences are GL's greater emphasis on audit committees (see Rasmussen and Schmidt 2012), on penalizing the chair (rather than all members) of key committees, on directors' performance at other firms, as well as a different methodology in assessing pay-for-performance (see Ertimur et al. 2013) and a tighter threshold for board independence (two thirds of the board rather than a majority). For more details, see Glass Lewis & Co. (2011).

releases to its clients before the annual meeting detailing its voting recommendations and their rationale. We read the relevant sections of the report to identify and categorize the reason(s) for the negative recommendation.[15] We turn to such analysis next.

2.2 The rationale behind ISS recommendations: a categorization

Based on our reading of the ISS reports, we group negative ISS recommendations into three broad categories, depending on whether they are issued for an individual director (*Individual)*, every member of a committee (*Committee)* or every member of the board (*Board)*.

Individual-level issues pertain to concerns with one specific director, which we further partition into three main sub-categories (chosen because most frequent in our sample): independence-related concerns (*Independence*), failure to attend at least 75% of the board meetings without a valid reason (*Attendance*) and director sitting on too many other boards (*Busyness*), with the remaining (less frequent) categories grouped as *Other*. Within *Busyness*, we differentiate between CEOs (*Busy: 3+ Seats & CEO*) and other directors (*Busy: 6+ Seats*), because ISS applies different thresholds for directors who hold a CEO position in another firm (a CEO-director is deemed "busy" if she sits on more than three board seats, versus six for non-CEO directors). The *Independence* category includes cases where ISS recommends against affiliated or inside directors because they sit on a key committee (and, thus, potentially compromise its independence), or because the firm does not have a separate independent nominating committee or a majority-independent board.

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[15] Ideally, we would like to scrape and code the information in ISS reports for a broader sample of firms. However, the ISS reports do not present the information about the rationale behind each recommendation in a standardized fashion across firms and over time. Extracting the rationale often requires a specialized knowledge of the respective governance provision as well as reading other parts of the reports or other documents (e.g. proxy statements). Because the organization of the information is not amenable to the use of text extraction programs, we limit the sample and conduct the coding ourselves.

For committee-level withholds, we differentiate between those targeting *Compensation Committee* members and those targeting audit or nominating committee members (*Audit & Nominating Committee*) (there are no cases of other committees targeted by negative recommendations in our sample). We further partition the *Compensation Committee* category into withholds that stem from a *Pay & Performance Disconnect*, *Poor Pay Practices* or *Other* compensation-related issues. ISS assesses *Pay & Performance Disconnect* based on its proprietary methodology, which includes a quantitative assessment of the historical correlation of pay and performance and a qualitative analysis of the factors behind any disconnect. The most frequent examples of *Poor Pay Practices* include certain terms of the severance package (excise tax gross-ups, modified single trigger arrangements), excessive perquisites and tax gross-ups on perks, and, to a lesser extent, one-time awards (discretionary bonuses, special grants, retention packages, etc.). *Other* includes mostly cases of option backdating (analyzed by Ertimur, Ferri and Maber 2012).

Finally, we classify concerns that lead to ISS withhold recommendations from all directors up for election (*Board* category) into three groups: *Lack of Responsiveness* (e.g., the board did not implement a shareholder proposal that either received support from the majority of the shares outstanding at the previous year's meeting or received support from the majority of shares cast at the two previous annual meetings), *Poison Pill* (e.g., the board adopted or renewed a poison pill without shareholder approval), and *Other*. Appendix 1 includes a more complete description of the criteria used by ISS over our sample period as well as the key subsequent changes.

As important as the reasons behind ISS recommendations (and thus shareholder votes) are the factors that do not appear to play a role. Recent research highlights the importance of directors' skills sets (Adams et al. 2013), their advising quality (Coles et al. 2012; Faleye et al. 2011), their technical expertise (DeFond et al. 2005) and their industry expertise (Faleye et al. 2013; von

Meyerinck, Oesch and Schmid 2015). Recent regulation requires firms to provide more information about why the nominees are suited to serve on their board.[16] However, proxy advisors do not try to assess whether individual directors and boards as a whole have the right level of expertise and skills, probably because of the difficulties in developing voting recommendations around these issues. This is evidenced by the fact that proxy advisors generally recommend in favor of new directors up for election and exempt them from negative recommendations issued against incumbent directors. Also, recent studies question the traditional view that more independent boards and less "busy" directors are necessarily better (Adams and Ferreira 2007; Masulis and Mobbs 2011; Field, Lowry and Mkrtchyan 2013) and offer new ways of thinking about director independence (e.g., the fraction of directors appointed after the CEO, or "co-opted" directors, see Coles, Daniel and Naveen 2014). The examination of whether and how proxy advisors will incorporate these new insights into their voting policies is a fruitful area for future research.

2.3 The rationale behind ISS recommendations: frequency and association with voting outcome

Table 3 presents the frequency of the reasons behind ISS withholds and their association with the voting outcome and thus provides some insights into the relative importance of the factors shareholders focus on when voting in uncontested director elections. Because some directors receive a withhold for multiple reasons, the 1,673 director-firm-years with a withhold (Table 1) translate into 1,762 unique withholds (our inferences are similar if we focus only on directors who receive a withhold for a single reason). There are 664 individual-level, 580 board-level and 497 committee-level withholds in our sample (representing, respectively, 38.1%, 33.3% and 28.6% of

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[16] In December 2009, Regulation S-K was amended to require firms to provide more detail about the rationale for nominating a given director (in particular, Item 401(e) states: "briefly discuss the specific experience, qualifications, attributes or skills that led to the conclusion that the person should serve as a director … in light of the [firm]'s business and structure. If material, this disclosure should cover more than the past five years, including information about the person's particular areas of expertise or other relevant qualifications").

the total).[17] About two-thirds of the individual-level withholds relate to *Independence* issues (with *Busyness* and *Attendance* comprising most of the other cases). Almost all the committee-level withholds refer to the *Compensation Committee*. *Poor Pay Practices* are the leading reason for compensation-related withholds (318 cases), followed by *Pay & Performance Disconnect* (119 cases). This contrasts with the recent say on pay votes (Ertimur et al. 2013), where a perceived pay-for-performance disconnect is the reason for 73% of the negative ISS recommendations. As for board-level withholds, 419 cases out of 580 (72.2%) relate to *Lack of Responsiveness* to majority-vote shareholder proposals. Among these proposals, the most common are proposals to (*i*) declassify the board (60.2% of the sample), (*ii*) submit a poison pill to shareholder approval (21.6%) and (*iii*) eliminate supermajority voting requirements (19.4%; untabulated analysis).

Splitting the sample period between 2003-2006 and 2007-2010 (so as to compare two periods of equal length) reveals key shifts in the frequency of withhold reasons. In particular, the frequency of compensation-related withholds has increased from 7.0% (54 out of 760) to 41.8% (419 out of 1,002) of the sample, becoming the most frequent category and exemplifying the growing concerns with executive pay that eventually led to the introduction of mandatory say on pay votes in 2011 (Ertimur, Ferri and Muslu 2011). In contrast, the frequency of independence-related withholds has dropped from 38.8% to 14.2%, likely because firms began to comply with NYSE and NASDAQ new listing requirements related to board independence (Chhaochharia and Grinstein 2007).

With regard to the association with voting outcomes, Table 3 shows substantial variation in voting outcomes both across categories (e.g. board-level withhold recommendations garner the

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[17] Individual-, committee- and board-level withholds add up to 1,741 rather than 1,762 because in cases where a director receives a withhold for more than one reason within the individual-, committee- or board-level category, we treat it as one withhold at the individual-/committee-/board-level. For example, if a director receives a withhold for poor attendance and for sitting on too many boards, we count it as one individual-level withhold.

highest mean votes withheld, 29.70%) and within each category (e.g. within board-level issues *Poison Pill* withholds are associated with the highest mean votes withheld, 32.85%).[18]

To shed light on the determinants of the variation in voting outcomes, we estimate a series of multivariate models, using the same control variables as in Table 2. We make two predictions. First, we conjecture that the percentage of votes withheld will increase in the severity of the concerns underlying the vote. In particular, we predict that voting shareholders will be more concerned (and more likely to vote in line with ISS recommendations) when the director receives a withhold for multiple reasons (rather than a single reason) and when the rationale behind the withhold is a board- or committee-level issue (rather than an individual-level issue)—more likely to be a symptom of a dysfunctional board. Table 4, Model 1 shows that votes withheld are indeed, on average 4.79% higher when a director receives a withhold for multiple reasons (the coefficients of *ISS Withhold–Single Reason* and *ISS Withhold–Multiple Reasons* are 0.2047 and 0.2526, respectively, with the difference significant at 1%). Model 2 shows that the sensitivity of shareholder votes to the ISS recommendation is highest for board-level issues (coefficient of 0.2548), followed by committee- (0.1973) and individual-level issues (0.1644) (the differences between the three coefficients are significant at 1% level), consistent with the pecking order suggested by Table 3. The same holds when we further split the individual-, committee- and board-level ISS recommendations into more specific categories (e.g., independence, busyness; untabulated tests). For example, the coefficient of interest ranges from 15.42% for independence-related individual-level ISS withhold recommendations to 29.32% for poison pill-related board-level ISS withhold recommendations.

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[18] Table 3 also reveals a general increase in votes withheld across all categories (except *Independence*), consistent with the evidence of greater activism via voting in the second half of the sample period (Ferri 2012).

Second, we conjecture that, in deciding whether to follow ISS recommendations, shareholders will also take into account contextual factors other than the recommendation itself and its rationale. In particular, shareholders will be more inclined to vote with ISS on a specific issue when they are already concerned with the governance structure of the firm, as proxied for by a high level of the entrenchment index (Bebchuk, Cohen and Ferrell 2009) and the presence of excess CEO pay (Core, Holthausen and Larcker 1999). In Models 3 and 4 we find that the coefficient of *ISS Withhold* is significantly higher (by 5.4% and 2.3%, respectively) at firms where the entrenchment index is above the sample median and at firms with positive excess CEO pay.[19]

Overall, it appears that shareholders take into account the severity of the underlying problem as well as other contextual factors before casting their votes. We will discuss the implications of this finding in the next section.

2.4 Discussion of findings and implications for the policy debate

2.4.1 Interpreting the association between ISS recommendations and shareholder votes

While our main objective is to examine the factors behind shareholder votes in uncontested director elections and the effectiveness of these votes in triggering governance changes, it is useful to assess the implications of our findings for the debate on the role of proxy advisors.[20] Previous studies have suggested three (not mutually exclusive) explanations for the positive association between ISS recommendations and shareholder votes (e.g. Choi et al. 2010). First, ISS recommendations simply coincide with shareholder preferences over governance issues. Under this view, the association reflects the percentage of votes cast by shareholders who do independent research (and thus cast an informed vote) and happen to arrive at the same conclusion as ISS on a

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[19] In untabulated analyses, for the subset of observations with GL data we replicate the tests in Table 4 by including an indicator denoting a GL withhold. Our inferences are unchanged.

[20] Critics have called for greater regulation of the proxy advisory industry, expressing concerns with limited industry competition, lack of transparency and potential conflicts of interests (see Choi et al. 2010; SEC 2010, 2013, 2014).

given topic. Malenko and Shen (2015) effectively rule out this explanation. Malenko and Shen (2015) exploit a cutoff rule in ISS' 2011 say on pay voting guidelines and, using a regression discontinuity design, estimate the effect of ISS recommendations to be 25%. This is virtually identical to the ordinary least squares (OLS) estimate, suggesting an omitted variable bias close to zero. In other words, OLS associations (of the type reported in this study) do not simply capture the extent to which ISS and voting shareholders independently develop the same voting guidelines.

The second explanation is that the association captures the percentage of votes cast by shareholders who blindly follow ISS recommendations because it is a cost-effective way to fulfill their fiduciary duties—that is, the association captures the percentage of uninformed votes effectively outsourced to ISS.[21] In numerous public statements, the SEC has repeatedly embraced this view and noted ISS's "outsized influence" (e.g. Gallagher 2014).

Our findings in Tables 3 and Table 4 cast doubt on the descriptive validity of this explanation. If the association entirely reflected the percentage of shares some investors mechanically vote in line with ISS, then the sensitivity of shareholder votes to ISS recommendations would either be "fixed" across firms (assuming similar ownership composition) or only vary with their ownership composition (i.e. would be higher in firms where shareholders outsourcing their votes to ISS control a greater percentage of votes). Instead, Tables 3 and 4 show that the association varies in a systematic way with the rationale behind the recommendation, the severity of the underlying problem or other circumstances (e.g., firm's governance structure). To ensure that the variation does not just stem from differences in ownership composition, in

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[21] In the words of Leo Strine, former vice chancellor of the Delaware Court of Chancery, some institutional investors "simply follow ISS's advice rather than do any thinking of their own" (Strine 2005). Some commentators note that this behavior may be partly the result of a 2003 SEC rule, which requires mutual funds to vote in their clients' best interests and explicitly states that an institution could demonstrate that the vote was not a product of a conflict of interest if it voted client securities in accordance with a pre-determined policy, based upon the recommendations of an independent third party. (Proxy Voting by Investment Advisers, SEC Release No. IA-2106).

untabulated tests we examine firm-year observations where more than one director receives a withhold recommendation and for different reasons. We find, on average, an 11.2% difference between the highest and lowest votes withheld, suggesting that the *same* shareholders in the same firm decided to follow some, but not all, the ISS recommendations depending on their rationale and other factors, consistent with a certain degree of informed voting .[22]

The evidence in Iliev and Lowry (2015) cast further doubt on the SEC's view. These authors find that 25% of mutual funds (the only institutional investors required to disclose their votes) always vote in line with ISS but that these funds tend to be small and thus hold a small percentage of the total equities owned by mutual funds. The other funds tend to deviate repeatedly from ISS, with the extent of the deviation depending on the costs and benefits of informed voting.

In brief, the average association between ISS recommendations and shareholder votes is likely to significantly overstate ISS "causal" influence (in the sense of the extent of uninformed votes cast with ISS). One may try to estimate the extent of ISS causal influence by extrapolating the results from mutual funds' votes to other investors, or may use the lowest association between ISS recommendations and shareholders votes across various settings. But these estimates would only represent an *upper* bound of the extent of uninformed voting.

This is because there is a third, potential explanation of the association between ISS recommendation and shareholder votes: ISS recommendations synthesize and aggregate institutional investors' preferences. Starting in 2003, ISS has been developing its voting guidelines in consultation with its clients. In particular, a few months after each proxy season, usually in July-August, ISS sends a survey to its clients as well as corporate issuers and other interested constituencies, with a series of questions about specific governance issues and potential revisions

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[22] In their analysis of the option backdating scandal, Ertimur et al. (2012) report a similar difference in votes withheld between directors at the same firm who are targeted by negative ISS recommendations triggered by different reasons.

to its voting guidelines. At the same time, ISS hosts various roundtables with industry groups and collects informal feedback from various market participants. The results of the survey are publicly disclosed and become the basis for the release of new proposed voting guidelines for the following proxy season, which are eventually finalized in November after an open comment period.[23] Given the nature of this process, one cannot simply assume that shareholders who typically vote with ISS are casting uninformed votes, because at least some of them take an active role in developing the voting guidelines in the first place. For example, large institutional investors are more likely to respond to the survey. In brief, ISS recommendations can be viewed as reflecting the "consensus" of the largest institutional investors among its clients, making it difficult to exactly measure the extent of uninformed voting behind the documented associations.

2.4.2 *ISS's agenda setting role*

The above discussion implies that regulators' concerns that the association between ISS recommendations and shareholder votes entirely reflects uninformed voting is largely exaggerated. At the same time, however, our analysis highlights a subtle and more important form of proxy advisors' influence, largely neglected in the academic and policy debate: that is, their agenda-setting role. Absent a negative recommendation from either proxy advisor, cases of substantial voting dissent ae extremely rare, if any. As noted in Table 1, in all of the 18 cases where a director failed to receive majority support (i.e., votes withheld greater than 50%), both ISS and GL had issued a withhold. Even more remarkable, there is not a single instance of votes withheld above 20% a withhold recommendation by ISS or GL. These figures suggest that activist shareholders rarely rally other voting shareholders around issues not identified by the proxy advisors, or that

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they have limited success in doing so.[24, 25] This is a significant concern because, as noted earlier in Section 2.2, proxy advisors have not developed voting guidelines with respect to many issues of significant relevance to investors according to practitioners and recent research (e.g., board's overall expertise, individual directors' skill set and experience, fit with the rest of the board, etc.). Besides, some of their guidelines (e.g. independence, busyness) seem to be anchored to an old view of what constitutes "good" governance.

Thus, a key implication of our analysis for policy-makers and researchers is that proxy advisors' agenda setting role (the choice to focus on some governance issues and neglect others) is arguably more important than the effect of their recommendations on shareholder votes. Conditional upon a negative recommendation institutional investors do seem to investigate the issue before casting the vote, resulting in substantial and predictable variation in the sensitivity of votes withheld to the recommendations (or, in the language of Iliev and Lowry 2015, in the extent of deviations from ISS recommendations). But on the issues neglected by proxy advisors (e.g., due to lack of sophistication, or difficulty in developing voting policies), we observe the "shareholder passivity" that has characterized shareholder voting for many decades, arising from the classic collective action problem (Black 1990). This observation calls for more academic research on the process by which ISS develops its guidelines, and especially, on whether ISS's survey focuses on value-relevant issues and efficiently aggregates shareholders' preferences.

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[24] This is consistent with the low frequency of "vote-no" campaigns (i.e. campaigns to "withhold the vote" from board members organized by activist shareholders) in Del Guercio et al. (2008). In particular, Del Guercio et al. (2008) report that there were only 112 "vote-no" campaigns organized by activist shareholders among all US publicly traded firms between 1990 and 2003, averaging 11.4% votes withheld. Our findings imply that, to the extent that such campaigns persist in our sample period, they fail to trigger more than 20% votes withheld if not accompanied by a negative recommendation from the two most influential proxy advisors.

[25] Our conclusions are based on *aggregate* votes. Prior literature provides evidence of systematic heterogeneity in voting behavior among shareholders (Matvos and Ostrovsky, 2010). Thus, it is possible that some investors focus on issues that are neglected by proxy advisors. However, the votes of such investors do not seem to affect the aggregate voting outcome, on average.

3. Consequences of director elections: how do firms respond to adverse votes?

In this section, we examine how firms respond to high level of votes withheld.[26] We start by analyzing the relation between votes withheld and subsequent director turnover, which may be viewed as the most extreme form of responsiveness (removing directors singled out by voting shareholders). Then, exploiting our detailed data on the rationale behind withhold recommendations, we consider a less extreme form of responsiveness: directors' and firms' actions to address the problem that led to the adverse vote in the first place.

3.1 Votes withheld and subsequent director turnover

At most firms, in uncontested elections the percentage of votes withheld has no effect on the election outcome, and, thus, no mechanical impact on subsequent director turnover. This is because under the plurality voting standard a director nominee is elected as long as she receives one vote in favor, no matter how many votes are withheld (Norris 2004).[27]

However, several studies, across various settings (e.g., restatements, litigation, option backdating), provide evidence that poorly performing directors are more likely to turn over (Yermack 2004; Srinivasan 2005; Ertimur et al. 2010, 2012). To the extent that a high percentage of votes withheld is a proxy for (shareholders' perceptions of) poor performance, one may expect

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[26] Del Guercio et al. (2008) also examine firms' responsiveness to shareholder votes in uncontested director elections, but only in the context of "vote-no" campaigns organized by activist shareholders between 1990 and 2003. Vote-no campaigns are fairly rare (112 in their sample period) and the authors identify the underlying reason and the subsequent firm response only for a subset of the campaigns (54 cases). Also, most of these campaigns call for operational improvements, while governance reform is an objective only in about half of them. In contrast, we examine all cases of significant voting dissent in uncontested director elections and for a more recent sample period, when activism via voting has become more frequent and has focused on a different set of governance issues. Also, we perform a series of multivariate analyses to ascertain whether the firm's actions are "abnormal" and likely driven by the prior shareholder vote.

[27] As noted earlier, under the "plurality plus resignation" standard recently adopted by many S&P 500 firms, while a nominee with less than 50% of the votes must resign from the board, the director is technically elected and will not turn over unless the board accepts her resignation (Allen 2007; Cai, Garner and Walkling 2013; Ertimur et al. 2015). Only at the relatively few firms adopting a true "majority voting" standard a director receiving less than 50% of the votes in favor is technically not elected. In our sample none of the directors with more than 50% votes withheld sit on boards of majority voting firms. Hence, empirically there is no mechanical relation between votes withheld and subsequent director turnover. Regardless of the level of votes withheld, whether a negative vote will trigger director turnover is ultimately a board's decision.

that directors receiving high votes withheld are similarly more likely to turn over. To examine this question, we estimate the following director-level logistic regression:

Director Turnover = α_0 + α_1*Votes Withheld* + β*Controls* + ε (2)

The dependent variable, *Director Turnover*, is an indicator variable equal to one if the director turns over between the year *t* and year *t+1* meeting. The variable of interest, *Votes Withheld*, is the percentage of votes withheld from the director at the year *t* meeting. Following prior studies (e.g., Yermack 2004; Ertimur et al. 2012) we control for a number of director and firm characteristics (see Table 5 for details) and include year and industry fixed effects.

Table 5, Model 1 reports the results. The association between *Votes Withheld* from a director and subsequent turnover is positive and significant, but only at the 10% level. However, the economic significance of this result is low, with the predicted likelihood of turnover increasing from 6.2% to 7.1% when votes withheld move from 0.6% (5th percentile of the distribution) to 20.6% (95th percentile). Also, the association is not driven by cases of votes withheld above the 20% and 50% thresholds—the coefficients on the corresponding indicators in Models 2 and 3 are insignificant.[28] Finally, when we partition the data by the nature of the recommendation in Model 4 (single vs multiple withhold; board- vs. committee- vs. individual-level), we do not find a stronger association when the concern is more severe.[29]

Overall, we conclude that there is little evidence of any effect of shareholder votes in uncontested director elections on subsequent director turnover not only in terms of "average"

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[28] We focus on the 20% threshold because it is usually viewed as a sign of significant dissatisfaction with directors (Del Guercio et al. 2008; Ertimur et al. 2012) and on the 50% threshold to examine whether turnover is more likely after a negative majority vote. Only two of the 18 directors with votes withheld greater than 50% (see Table 1 Panel C) turn over. In both cases, our reading of the relevant 8-K filing suggests that turnover is not related to the vote (e.g., a director is replaced in compliance with a merger agreement).

[29] As for the control variables, consistent with earlier studies (e.g., Ertimur et al. 2014), there is a higher likelihood of turnover after a change in CEO, when the director is older than 65 and has longer tenure, and lower likelihood when the director is the CEO of the firm, for new directors, for independent directors, and in firms with classified boards.

effect (similar Cai et al. (2009) for an earlier sample period) but also conditional on proxies for severity of the concerns behind the adverse vote.

Following prior studies on the director labor market (Fama 1980; Fama and Jensen 1983; Srinivasan 2005; Fich and Shivdasani 2007; Ertimur et al. 2010), in untabulated tests we examine whether votes withheld are associated with a net decrease in the number of other seats held at publicly traded firms in the US (data source: BoardEx). Using the same specifications as in Table 5, we generally find no evidence of a systematic relation between votes withheld from a directors at a given firm and subsequent change in the number of other seats held by that director.

3.2 Firms' response to negative votes and their rationale: descriptive evidence

The analysis above suggests that high votes withheld from a director do not generally result in the director losing her seat or seats held at other firms. A potential explanation for these results is that firms respond by addressing the concerns that underlie the vote, eliminating the need for labor market penalties.

To measure firms' responsiveness to the concerns underlying the vote, as a first step we examine whether directors receive a "repeated" withhold for the same reason at the subsequent annual meeting. We interpret the lack of a repeated withhold as evidence of responsiveness.[30] As we discuss below, this interpretation is not always valid. Hence, as a second step we obtain and read the ISS report in year *t+1* and directly verify, case-by-case, whether the director or firm took concrete actions to remove the problem underlying the vote in year *t*.

Table 6 summarizes the results of this analysis. The first column reproduces the figures in Table 3, but, to ensure that a repeated withhold is truly triggered by the *same* concern as the previous year, with a more granular breakdown of the withhold rationales (particularly in the

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[30] The percentage of votes withheld after the first withhold and after a repeated withhold is similar (untabulated analyses). Hence, a repeated withhold can be viewed as a proxy for shareholder concerns that remain unaddressed.

Independence category).[31] Because responsiveness is defined at the firm-level, in the case of committee- and board-level recommendations we collapse the number of director-year-level observations (from Table 3) into a number of firm-year level observations, reported in parenthesis (e.g., 318 cases of *Poor Pay Practices* collapse into 107 firm-year level observations).

The second column reports the number of observations for which we are able to obtain information regarding the occurrence of a withhold in year $t+1$ and the actions taken by the director or firm after the year t withhold. Comparing the second and first columns, we lose only a few observations for committee- and board-level cases, but substantially more for individual-level cases. This is mostly because for firms with a classified board structure, the director with a withhold in year t will not be up for election in year $t+1$, and, thus, we cannot observe whether the withhold is repeated or not.[32] If these directors are less responsive (because not up for election in $t+1$), or, more generally, if firms with classified boards are less responsive (Faleye 2007), we may overstate the rate of responsiveness to individual-level recommendations.

The third (fourth) column reports the number (percentage) of cases where the withhold is not repeated in the subsequent year. It appears that firms respond to most committee- and board-level recommendations, and to about half of the individual-level recommendations. However, lack of a repeated ISS withhold overstates true responsiveness for two reasons. The first has to do with ISS voting policies. Consider the *Poison Pill* category, where most withhold recommendations result from the board adopting a poison pill without shareholder approval during the previous year. ISS does not issue a repeated withhold in year $t+1$ even if the firm does not take any action. That

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[31] The more granular breakdown of the *Independence* category explains why the total number of independence-related recommendations in Table 5 (N=96+123+201+19+74+108=621) is higher than in Table 1, Panel C (N=437). The difference is due to directors who receive a withhold for multiple independence-related sub-categories in Table 5.
[32] Other reasons for the difference between the first and second column in Table 5 are turnover (for individual-level recommendations), and, in few cases, mergers or delistings.

is, the withhold is a one-time event in the year of the poison pill adoption.[33] Our examination of the *t+1* ISS reports shows that only in 15.8% of the cases (fifth column) the firm responded to the withhold by removing the pill or submitting it to shareholder ratification (the two actions that we consider as "responsive"), well below the 89.5% figure suggested by the lack of repeated withhold (fourth column). There is a similar issue for the *Lack of Responsiveness* category, where ISS recommends withholdings votes from the entire board for failure to implement a shareholder proposal supported by a majority of the shares cast for the last two years or a majority of the shares outstanding the previous year. For firms that do not implement the proposal, if shareholders do not re-submit it for a vote in year *t*, ISS will not issue a withhold recommendation in year *t+1* (without another majority-vote for the proposal in year *t*, in year *t+1* the ISS criteria for a withhold will not be met). When we examine each case to determine whether firms implemented the proposal underlying the withhold recommendation, we estimate the rate of responsiveness at 48.9%, again well below the 73.9% suggested by the lack of repeated withhold.

The second reason for the difference between the fourth and fifth columns is that in some cases without a repeated withhold there is actually a withhold for substantially, but not exactly, the same reason. For example, consider a director who receives a withhold for being an *Affiliated Director on AC* in year *t* but not in year *t+1* because she moves to the CC committee and receives a withhold as *Affiliated Director on CC*. This director would be classified as no repeated withhold in the third and fourth columns of Table 6. In such scenarios, we reclassify the firm as not responsive, resulting in lower estimates in the fifth column than in the fourth column.

The "Estimated Rate of Responsiveness" column represents our best attempt to classify as responsive only cases where the director or firm took actions to deal with the problem that caused

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[33] More precisely, as detailed in Appendix 1, there will be a repeated withhold only if the poison pill has a dead-hand feature, or if the first withhold triggers more than 50% votes withheld.

the negative vote. We present the estimated rate of responsiveness as a range when we are not able to clearly establish whether the firm was fully or partially responsive (Appendix 2 provides greater details about our estimation procedure for each category).

Overall, based on the evidence in Table 6, we estimate a rate of responsiveness ranging between 39.0% and 47.7%. This is a fairly high figure considering that only in a handful of cases the votes withheld from a director exceed 50% (see Table 3), and, thus, the majority of shareholders (in terms of votes cast) have not expressed concerns with the director.[34]

Table 6 also highlights substantial variation in the rate of responsiveness among the three categories of recommendation (individual-, committee- and board-level) and within each category. Some of this variation is likely to reflect differences in the cost of the actions required to address the concerns behind the vote. For example, the rate of responsiveness is the highest (100%) for *Attendance*, probably because it is not particularly costly both for the director and the firm to make sure that in the subsequent year the director attends more than 75% of the board meetings. In contrast, the rate of responsiveness is lowest for the *Poison Pill* category (15.8%). Presumably firms receiving a withhold for failure to submit a new poison pill to shareholder approval have deemed the benefit of the immediate introduction of a poison pill higher than the cost of a negative recommendation (which will not be repeated next year – see earlier discussion), so they are unlikely to remove the pill or submit it to shareholder ratification in response to a negative vote.

Another noteworthy finding in Table 6 is the 48.9% figure for *Lack of Responsiveness*, which implies that almost half of the previously ignored majority-vote shareholder proposals are

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[34] For comparison, over the period 1997-2004, Ertimur et al. (2010) report a rate of implementation of 31.1% for shareholder proposals supported by more than 50% of votes cast (with a peak of 40% in 2003-2004) versus only 3.2% for proposals receiving less than 50% of the majority vote. Del Guercio et al. (2008) examine 112 "vote-no" campaigns organized by activist shareholders and find that the board implements 22% of proponents' specific requests completely and an additional 15% partially. Brav et al. (2008) and Klein and Zur (2009) report an implementation rate of, respectively, 45% and 60% in a sample of hedge fund targets.

implemented after an adverse vote. This may not appear to be a high figure relative to the 40% implementation rate for majority-vote shareholder proposals reported by Ertimur et al. (2010) for 2003-2004, but the comparison is misleading. The 48.9% is based on a sample of firms that ignored a majority-vote shareholder proposal for one or two years (presumably, the least responsive firms). That these firms implement the same proposal after a withhold recommendation (in spite of the percentage of votes withheld being below 50%) suggests that directors listen to shareholder votes more carefully when those votes are about the directors themselves. Also, the distribution of the type of proposals implemented and not implemented is similar, with proposals to declassify the board as most frequent proposal in both groups (untabulated). Hence, the high rate of responsiveness is not driven by the implementation of less substantial proposals.

For the committee-level category, the high rate of responsiveness for *Pay & Performance Disconnect* (92.5%) results from our reliance on ISS's assessment (based on its proprietary methodology) of whether the firm fails the pay-for-performance test (i.e., we use the lack of a repeated ISS withhold as a proxy for responsiveness).[35] A more meaningful figure is the 56.9% estimate for *Poor Pay Practices*, remarkably close to the 55% rate of responsiveness to mandatory say on pay votes reported by Ertimur et al. (2013).

As a final note, we make two recommendations to ISS to improve their disclosures. First, *t+1* ISS reports should devote a section to explain how the firm responded to the concerns raised at time *t* and, if it did not, why ISS decided not to issue another withhold recommendation. Second, for negative recommendations resulting from specific transactions that cannot be easily "undone" (e.g., a one-time option grant for retention purposes), the ISS report should indicate what actions

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[35] We verify that these firms report a decrease in CEO pay while performing at the same level as their peers, whereas firms with a repeated withhold experience an increase in CEO pay while underperforming their peers (see Appendix 2). Hence, it is likely that the lack of a repeated withhold does capture (albeit with noise) an improvement in the pay-for-performance relation (and, thus, may be used as a proxy for firms' responsiveness).

the firm should take to be responsive to the issue going forward and hold the firm accountable with a repeated withhold if those actions are not taken.

3.3 Are firms' responses "caused" by the votes and their rationale?

Table 6 provides descriptive evidence on firms' responses to the concerns underlying negative votes (as proxied for by ISS recommendations). It is possible, though, that these responses would have occurred regardless of the votes withheld as a result of concurrent trends in governance practices. To assess this possibility, for each of the three types of recommendations in Table 6 (individual-, committee- and board-level) we devise a multivariate test to examine whether ISS withhold recommendations predict the documented changes in governance practices after controlling for other, known economic determinants of such changes.

The three analyses, focused on turnover on key committees, changes in abnormal CEO pay and board declassification, are detailed below.

Note that in these analyses we use ISS recommendations as a proxy for the percentage of votes withheld (in view of the strong association documented earlier). The advantage of doing so is that we can then use the rationale behind the recommendations as proxy for the concern underlying the vote. This allows us to examine whether a specific governance change (e.g. declassify the board) only/mostly occurs in response to a vote triggered by concerns with the classified board structure, but not in response to a vote triggered by other matters, strengthening the extent to which the association can be interpreted as a causal effect of the vote.

3.3.1   Independence-related concerns and subsequent turnover on key committees

In the case of individual-level recommendations we focus on the most frequent category, *Independence* (N=437; Table 3). As detailed in Appendix 2, firms respond to these concerns by removing directors with independence issues from a key committee. To examine whether the rate

of turnover from these key committees is unusually high subsequent to an independence-related vote, for each of the three key committees and for the sample of directors who sit on that committee at the year *t* annual meeting and are still on the board at the time of the year *t+1* meeting, we estimate the following logistic regression:

NC (CC, AC) Turnover = α_0 + α_1*ISS Withhold–Independence NC (CC, AC)* + β*Controls* + ε (3)

The dependent variable, *NC (CC, AC) Turnover*, is an indicator variable that is equal to one if the director sits on the nominating (compensation, audit) committee at the year *t* meeting and is still on the board but no longer on the nominating (compensation, audit) committee at the year *t+1* meeting. *NC (CC, AC) Turnover* is equal to zero if the director remains on the respective committee at the year *t+1* meeting. The variable of interest, *ISS Withhold–Independence NC (CC, AC)*, is an indicator variable equal to one if a director on the NC (CC, AC) receives an independence-related ISS withhold (a proxy for an independence-related high vote withheld).[36] We control for the presence of a non-independence related withhold recommendation as well as a number of director and firm characteristics (see Table 7 for detailed variable descriptions and data sources). We also include industry and year fixed effects.

Table 7 presents the results for the sample of directors on the NC, CC and AC (Models 1, 2 and 3, respectively). The coefficients of *ISS Withhold–Independence NC*, *CC* and *AC* are positive and statistically significant at the 1% level, suggesting that independence-related votes withheld (but not votes withheld driven by other factors; see the insignificant coefficient of *ISS Withhold–Non-Independence*) are associated with higher turnover from NC, CC and AC. The results are also economically significant. The likelihood of NC (CC, AC) turnover increases from 10.3% (10.2%, 11.5%) for directors without a withhold to 21.1% (19.1%, 23.5%) for directors with an

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[36] Essentially, the sample used in this test is represented by the first four rows in Table 5: *Affiliated Director on AC (CC, NC)* and *Insider Director on NC*.

independence-related withhold, holding all continuous (binary) control variables at their mean (median).[37] Combined with the evidence in Table 5, this analysis suggests that while high votes withheld do not affect director turnover they may induce significant turnover on key committees.

3.3.2   Compensation-related concerns and change in abnormal CEO compensation

Next, we focus on compensation-related recommendations (the most frequent sub-category of committee-level withholds; see Table 3). It is not clear whether the responsiveness to compensation-related withholds Table 6 documents is related to the vote per se or is the result of a general trend (e.g., increasing pay-performance sensitivity, removing certain practices). We adopt a "catch-all" approach used in previous literature (e.g., Core, Guay and Larcker 2008; Cai et al. 2009; Ertimur et al. 2011) and examine whether there is a change in abnormal CEO pay (the portion of CEO pay not predicted by known economic determinants) around the event of interest— a compensation-driven vote, as proxied for by a compensation-related ISS withhold—, after controlling for other factors that may explain such change. We estimate the following firm-year-level ordinary least squares regression for our sample firms:

Change in CEO % Residual Pay = α_0 + α_1 *ISS Withhold–Compensation* + β*Controls* + ε (4)

The dependent variable, *Change in CEO % Residual Pay* is the difference between *CEO % Residual Pay* in year *t+1* and year *t*. *CEO % Residual Pay* is defined as the natural logarithm of *CEO Total Pay* less the natural logarithm of *CEO Predicted Pay*. Therefore, *Change in CEO % Residual Pay* captures the change in percentage abnormal CEO pay between *t* and *t+1*.[38] The

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[37] The results are similar when we limit the sample period to 2005-2010 to exclude the effect of changes in board composition induced by new NYSE and NASDAQ listing rules following the Sarbanes-Oxley Act in 2002 (Chhaochharia and Grinstein 2007). With respect to the control variables, there is some evidence that female directors and new directors are less likely to turn over, though the results vary across committees.

[38] Similar to Core et al. (2008), we compute *CEO Predicted Pay* by taking the exponent of the predicted value for each firm from a regression of the natural logarithm of total CEO compensation on proxies for economic determinants of CEO pay. In particular, we estimate the following annual cross-sectional regressions for all firms in the ExecuComp database: $ln(CEO\ Total\ Pay_t)$ = α_0 + $\alpha_1 ln(CEO\ Tenure_t)$ + $\alpha_2 ln(Sales_{t-1})$ + $\alpha_3 S\&P500_{t-1}$ + $\alpha_4 Book\text{-}to\text{-}Market_{t-1}$ + α_5 *Stock Returns*$_t$ + α_6 *Stock Returns*$_{t-1}$ + $\alpha_7 ROA_t$ + $\alpha_8 ROA_{t-1}$ + $\alpha_9 CEO\ Turnover_t$ + *Industry Fixed Effects* +ε where

variable of interest, *ISS Withhold–Compensation,* is an indicator variable that is equal to one if one

or more directors receive a compensation-related withhold at the year *t* meeting.

Table 8, Model 1 presents the results for a benchmark model without any control variables.

The coefficient of *ISS Withhold–Compensation* is negative and statistically significant at 1%,

suggesting a decrease in abnormal CEO pay following an adverse shareholder vote driven by

compensation-related concerns.[39]

In Model 2 we replace *ISS Withhold–Compensation* with three indicator variables that

capture its rationale in greater detail (along the lines of the breakdown in Table 3, and Table 6):

Pay-for-Performance, *Poor Pay Practices* and *Other*. The coefficients of *Pay-for-Performance*

and *Poor Pay Practices* are negative and significant (respectively, at 1% and 5%).

The focus on abnormal pay alleviates the concern that the changes in compensation are

driven by changes in firm characteristics over the same period. Nevertheless, in Model 3 we

include the CEO percentage abnormal pay for year *t* (*Lag CEO % Residual Pay*) to control for

mean reversion in abnormal CEO pay, as in Core et al. (2008) and in Model 4 we also control for

the presence of a non-compensation related high votes withheld (as proxied for by non-

compensation related ISS withhold) and for other types of activism (compensation-related

shareholder proposals; see Table 8 for details). Consistent with prior studies (Core et al. 2008;

CEO Tenure$_t$ is the number of years the CEO has been at his current position as of year *t*, *Sales$_{t-1}$* is the company sales during year *t*-1, *S&P500$_{t-1}$* is an indicator variable equal to one if the firm is in the Standard & Poor's 500 Index in year *t*-1, *Book-to-Market$_{t-1}$* is the book market of equity scaled by market value of equity at the end of year *t*-1, *Stock Returns$_t$* (*Stock Returns$_{t-1}$*) is the company's unadjusted stock return for year *t* (*t*-1), *ROA$_t$* (*ROA$_{t-1}$*) is income before extraordinary items scaled by average assets during year *t* (*t*-1). *CEO Turnover$_t$* is an indicator variable that is equal to one if the CEO of the firm turns over in year *t*. To alleviate the impact of outliers, we winsorize the compensation variables at the 1st and 99th percentiles.

[39] Cai et al. (2009) make the same inference in their analysis. However, lacking data on the rationale behind ISS recommendations, they proxy for compensation-related votes by focusing on votes withheld from compensation committee members in firms with abnormal CEO pay. While this is a reasonable approach, a compensation committee member may receive a negative recommendation for any of the non-compensation related reasons in Table 5. Hence, their approach may simply capture the effect of mean reversion in abnormal CEO pay rather than the effect of compensation-related withheld. Also, following the approach in Cai et al. (2009), Ertimur et al. (2011) fail to find a significant effect in a more recent sample period. We believe our research design is more powerful and provides robust evidence that compensation-related votes withheld affect abnormal CEO pay.

Ertimur et al. 2011), there is evidence of strong mean reversion in abnormal CEO pay, with a remarkable increase in the explanatory power of the model (adjusted R^2 increases from 0.5% to 28.6%), while the other controls are not significant. In Models 3 and 4 only the coefficient of *ISS Withhold–Pay-for-Performance* remains significant. Its coefficient in Model 4 (-0.1791, significant at the 5% level) translates to a $1.57 million reduction in total CEO pay, corresponding to 11.5% (16%) of the mean (median) CEO pay at these firms prior to the withhold recommendation.[40]

3.3.3 Lack of responsiveness to shareholder proposals to declassify the board and subsequent board declassification

Our third test focuses on board-level recommendations. The most frequent sub-category is *Lack of Responsiveness* to majority-vote shareholder proposals. Per Table 6, in 48.9% of the cases firms respond to these recommendations by implementing the (previously ignored) proposal. Yet, it is not clear whether the firms would have implemented the proposal anyway, perhaps as a result of a general trend toward the adoption of the governance provision requested by the proposal. We examine this question by focusing on a specific governance change, the declassification of the board. Partly fueled by increasing evidence of a negative association between classified boards and firms value (Bebchuk and Cohen 2005; Cohen and Wang 2013), shareholder proposals to declassify the board have been among the most frequent and successful (in terms of voting

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[40] The predicted value of *Change in CEO % Residual Pay* is -0.1629 when we set *ISS Withhold–Pay-for-Performance* to one, *ISS Withhold–Compensation–Poor Pay Practices* and *ISS Withhold–Compensation–Other* to zero, *Lag CEO % Residual Pay* to its mean value, and all other variables to their median values. The median value for the ratio of *Lag CEO Total Pay* to *Lag CEO Predicted Pay* for firms with *ISS Withhold–Pay-for-Performance* equal to one is 1.78. It follows that the predicted median ratio of *CEO Total Pay* to *CEO Predicted Pay* in year *t+1* is 1.51 (=e$^{-0.1629}$ × 1.78). Since the median *Lag CEO Predicted Pay* for firms with *ISS Withhold–Pay-for-Performance* equal to one is $5.8 million, the reduction in the ratio translates to roughly a $1.57 million reduction in total CEO compensation in year *t* + 1[= (1.78 − 1.51) × $5.8 million]. In essence, we find that in these firms CEO pay was 1.78 times the level justified by economic determinants before the withhold and only 1.51 times after the withhold.

support) over the last decade (Georgeson 2013). Indeed, they comprise 60.2% of the proposals underlying withhold recommendations due to *Lack of Responsiveness*.

To examine the effect of a withhold on the probability of declassifying the board, we estimate the following firm-year level logistic regression over the period 2003-2010 for all S&P 500 firms with a classified board in place at the time of the year t annual meeting:

$$Declassify\ Board = \alpha_0 + \alpha_1\ ISS\ Withhold–Failure\ to\ Declassify + \beta Control\ Variables + \varepsilon \qquad (5)$$

The dependent variable, *Declassify Board* is an indicator equal to one if the firm takes action to declassify during the year subsequent to the year t annual meeting. As a proxy for classified board-related high votes withheld, our variable of interest, is *ISS Withhold–Failure to Declassify,* an indicator variable equal to one if the firm's directors receive a *Lack of Responsiveness* withhold at year t for failure to implement a shareholder proposal to declassify the board. We control for firm characteristics potentially associated with the likelihood of declassifying the board (firm performance, board independence, board ownership; see Table 9 for details). We also include an indicator variable equal to one if the firm's directors receive high votes withheld at year t for any other reason (*ISS Withhold Rec–All Other*).

Table 9 presents the results. The coefficient of *ISS Withhold–Failure to Declassify* is positive and statistically (at the 1% level) as well as economically significant: based on Model (2), the likelihood of declassifying the board increasing from 5.5% to 39.5% (holding all other variables at their mean) in response to classified board-related votes withheld, a more than seven-fold increase. The coefficient of *ISS Withhold Rec.–All Other* is also positive and significant, but much smaller in magnitude. Poorly performing firms are more likely to declassify the board, while board independence and ownership do not seem to play a role.

3.3.4 Summary

While ascertaining causality in our setting is difficult, overall the analyses in Table 7-9 suggest that the governance changes documented in Table 6 are likely to be a direct response to the votes withheld, since they obtain only when that specific governance change is the reason behind the vote, rather than in response to all cases of high votes withheld. Thus, withholding votes from directors up for election (even below 50%) may be an effective mechanism in inducing governance reform. It remains possible that the actions we observe are driven by institutional investors' pressure subsequent to the vote, rather than the vote itself. However, because the governance changes we document address the issues underlying the negative vote, we can conclude that, at a minimum, the shareholder vote acted as a focal point to elicit the given change.

3.4 Firms' responsiveness; determinants and effects on performance

We conclude our investigation by examining the determinants and consequences of firms' responsiveness to negative recommendations and votes withheld. We start by collapsing the data in Table 6 to the firm-year level. In particular, we classify firm-years with one or more withhold recommendations as responsive if the firm responds to at least one of the withhold recommendations received in that year, and unresponsive if the firm does not respond to any.[41] We then compare responsive and unresponsive firms in terms of their characteristics at the time of the vote (determinants analysis) and their subsequent performance (consequences analysis).

Table 10, Panel A presents the results for the determinants analysis. We estimate a logistic regression for the likelihood of being responsive to a withhold as a function of shareholder pressure and controls for size, performance and governance structure. Our proxies for shareholder pressure are the highest percentage of votes withheld from any director in that firm-year (*Max Votes Withheld*) in Model 1, an indicator denoting multiple withhold recommendations in the same

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[41] For individual-level recommendations where the rate of responsiveness is defined in terms of a range (see Table 5), we use the upper bound of responsiveness in this Section. Results are similar when we use the lower bound.

firm-year (*Multiple Withholds*) in Model 2 and both variables in Model 3. Similar to prior studies

(e.g., Ertimur et al. 2010 in the context of responsiveness to shareholder proposals) across the three

models there is a positive association between shareholder pressure and the likelihood of

responsiveness. Our results are also economically significant. In Model (3), holding all other

variables at their mean, as the percentage of votes withheld increases from 11.6% to 61.7% (from

the 10th to the 90th percentile of the sample distribution), the likelihood of responsiveness increases

from 47.4% to 66.7% when *Multiple Withholds* is equal to zero and from 58.1% to 75.5% when

Multiple Withholds is equal to one. We also find that poorly performing firms are more likely to

respond to shareholder pressure.

While a number of studies have documented firms' responsiveness to shareholder votes in

various settings (Del Guercio et al. 2008; Ertimur et al. 2010, 2013; Ferri and Maber 2013), there

is little evidence on its implications on firm performance and the question of whether greater

shareholder voice has a positive or negative effect on firm value remains open to debate (Larcker

et al. 2011; Cuñat et al. 2012; Ferri and Maber 2013).[42] In Panel B we take a step toward filling

this gap by comparing the subsequent performance of responsive and non-responsive firms. In

particular, we examine changes in industry-adjusted ROA (after controlling for the pre-withhold

level of industry-adjusted ROA), changes in industry-adjusted Tobin's Q (after controlling for the

pre-withhold level of industry-adjusted Tobin's Q) and abnormal returns (see notes to Table 10 for

more details). We do not find any evidence of a significant difference in performance between

responsive and non-responsive firms. To examine whether greater responsiveness (or

responsiveness to issues of greater concern to shareholders) has a differential effect on

performance, we perform three additional tests (untabulated). First, we re-define as responsive

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[42] Del Guercio (et al. (2008) analyze the performance implications of responsiveness to vote-no campaigns between 1990 and 2003, but their sample size is quite small (only 19 responsive firms).

only firms responding to *all* (rather than at least one of the) withhold recommendations in a given year. Second, we re-define as responsive only firms responding to board-level withhold recommendations (or, alternatively, board-level and committee-level recommendations). Third, we introduce an interaction term between the responsiveness indicator and an indicator equal to one if votes withheld are above the sample median (a proxy for more severe problems). These additional tests again fail to detect a differential effect on performance.

Overall, our findings suggest that greater responsiveness to shareholder votes on director elections is associated with neither superior nor inferior subsequent performance. One explanation is that the items pushed by proxy advisors and voting shareholders in the context of uncontested director elections have little effect on firm value (see Section 2.2), consistent with claims that activists misdirect their efforts towards "symbolic" corporate governance issues (Kahan and Rock 2014). An alternative explanation is that firms optimally decide when to and when not to respond to shareholder pressure, leading to no performance differences. Under both interpretations, it does not appear that mandating or inducing greater responsiveness to shareholder votes would be value enhancing, at least in the context of uncontested director elections. Examining this question using a broader definition of responsiveness to shareholder votes (including other management proposals, say on pay votes, shareholder proposals) is a promising avenue for future research.

4. Conclusion

We open the "black box" of director elections and shed light on the factors driving shareholder votes as well as the direct effect of these votes on firms' actions, using the rationale behind ISS recommendations as a proxy for the reason behind shareholders' votes. First, we validate this proxy in a comprehensive sample of 23,844 director-firm-year observations for uncontested director elections held at S&P 500 firms over the 2003–2010 period—there is an

almost one-to-one mapping between high shareholder dissent and ISS recommendations. Second, we analyze the frequency of the reasons behind ISS withhold recommendations and their association with the voting outcome to provide insights in the relative importance of the factors shareholders focus on when voting in uncontested director elections. We find substantial variation in the level of votes withheld from directors conditional on the underlying reason.

Next, we examine the specific actions firms take to address the concerns underlying the negative votes, using the information in the ISS reports to proxy for these concerns. The rate of responsiveness ranges between 39.0% and 47.7%, with substantial variation across individual-, committee- and board-level recommendations, as well as within each category. While ascertaining causality in our setting is difficult, multivariate tests suggest that the documented governance changes are a direct response to the votes withheld and, thus, uncontested director elections may be an effective mechanism in inducing governance reform. Our evidence of firms' responsiveness to the votes also helps explain the lack of association between votes withheld and subsequent director turnover. Shareholders use their votes on uncontested director elections to get boards to listen to and address specific problems, rather than to vote directors off the board.

Finally, we compare determinants and performance consequences of responsiveness. We find that firms are more likely to respond to votes withheld when shareholder pressure is higher and when performance is lower. However, responsive and non-responsive firms do not differ in terms of subsequent performance. Our study contributes to the literatures on director elections and on shareholder voting, as well as to the broader research on shareholder activism and the policy debate on enhancing shareholder voice.

Appendix 1: Summary of 2003-2010 ISS Proxy Voting Guidelines[*]

ISS voting recommendations on director nominees in uncontested elections focus on four areas: director independence, director competence, board responsiveness and board accountability.

Director independence: ISS recommends withholding votes from inside directors and affiliated outside directors in the following cases: (i) they serve on any of the three key committees (audit, compensation, nominating); (ii) the firm lacks an audit, compensation or nominating committee so that the full board functions as that committee; (iii) the firm lacks a formal nominating committee (even if the board attests that the independent directors fulfills the functions of such a committee); or (iv) the full board is less than majority independent. The ISS voting guidelines include a detailed description of what constitutes an inside director vs. affiliated outside director vs. independent outside director (ISS 2010, pp.14-16). Voting guidelines on director independence were in place throughout the entire sample period (2003-2010), except for (iii) (added in 2007) and (iv), which was added in 2004 in response to new NYSE and NASDAQ listing rules. In 2004, ISS also clarified the definition of inside and affiliated directors to include a broader number of relationships.

Director competence: ISS recommends withholding votes from individual directors who: (i) sit on more than six public company boards; (ii) are CEOs of public firms and sit on the boards of more than two public companies besides their own (withhold only at their outside boards); or (iii) attend less than 75% of the board and committee meetings without a valid excuse (illness, work on behalf of the company, service to the nation, funeral obligations). If the company provides meaningful private or public disclosures explaining the director's absence, ISS will evaluate the information on a case-by-case basis taking into account patterns of absenteeism, degree to which absences were due to an unavoidable conflict and other extraordinary circumstances underlying the director's absence. Voting guideline (iii) was in place throughout the entire sample period (2003-2010), while (i) and (ii) were added, respectively, in 2004 and 2005.

Board responsiveness: ISS recommends withholding votes from the entire board (except new nominees, who will be considered on a case-by-case basis) if: (i) the board failed to act on a shareholder proposal that received approval by a majority of the shares outstanding the previous year; (ii) the board failed to act on a shareholder proposal that received approval by a majority of the shares cast for the previous two consecutive years; (iii) the board failed to act on takeover offers where the majority of the shareholders tendered their shares; or (iv) at the previous board election, any director received more than 50% withhold/against votes of the shares cast and the company has failed to address the issue(s) that caused the high withhold/against vote. Voting guidelines on board responsiveness were in place throughout the entire sample period (2003-2010), except for (iv), which was added in 2005.

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[*] Source: authors' summary based on the annual ISS Proxy Voting Guidelines released between 2003 and 2010.

Board accountability:

Committee-level (Audit Committee, AC): ISS recommends withholding votes from all AC members if: (i) non-audit fees paid to auditors are excessive;[†] (ii) the firm receives an adverse opinion on the firm's financial statements from its auditor; or (iii) there is persuasive evidence that the AC entered into an inappropriate indemnification agreement with its auditor that limits the ability of the company, or its shareholders, to pursue legitimate legal recourse against the audit firm. Only voting guideline (i) was in place throughout the entire sample period (2003-2010), with (ii) and (iii) added, respectively, in 2009 and 2007. Starting in 2006, ISS may also recommend withholding votes from the AC (and potentially the full board), on a case-by-case basis, in presence of poor accounting practices manifested in fraud, misapplication of GAAP or material weaknesses under Section 404, depending on the severity of the case and the firm's efforts at corrective actions.

Committee-level (Compensation Committee, AC): ISS recommends withholding votes from all CC members (and potentially the full board in egregious cases) if: (i) there is a negative correlation between CEO pay and firm performance; (ii) the company has problematic pay practices; (iii) the firm fails to fulfill the term of a burn rate commitment made to shareholders; (iv) the firm fails to submit one-time transfers of stock options to a shareholder vote; or (v) the firm reprices underwater options without shareholder approval (even if allowed in the firm's equity plan).[‡] Voting guideline (i) was put in place in 2004, guidelines (ii)-(iv) in 2006 and (v) in 2007. Starting in 2010, ISS may also recommend withholding votes from all CC members if the board exhibits poor communication and responsiveness to shareholders on compensation-related issues (e.g., failure to respond to majority-supported shareholder proposals on executive pay).

Board-level, anti-takeover-related: ISS recommends withholding votes from the entire Board (except new nominees, who will be considered on a case-by-case basis) if: (i) the company's poison pill has a "dead-hand" or "modified dead-hand" feature; (ii) the board adopts a "long-term" (term >12 months) pill or renews any existing pill (long- or short-term), without shareholder approval;[§] however, a commitment to put a newly adopted pill to a binding shareholder vote may result in a positive ISS voting recommendation; or, (iii) the board makes a material adverse change

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[†] According to the 2010 ISS US Proxy Voting Guidelines, non-audit fees are excessive if they exceed the sum of audit fees, audit-related fees and tax compliance/preparation fees (fees for other tax-related services should be included in the non-audit fees). Examples of fees in each category or that may be excluded from the computation are provided. This policy has been in place since 2003, with the tax/compliance preparation fees included in the calculation since 2006.

[‡] The evaluation of the pay-performance link under (i) is based on a qualitative assessment of the historical alignment between CEO pay and stock performance (especially for poorly performing firms) over the past five years, with emphasis on the sources of increases in CEO pay, the composition of pay (i.e. extent of performance-based pay), the quality of disclosures, recent actions taken to increase pay-for-performance, etc. As for (ii), the guidelines provide a long list of examples of problematic pay practices, including certain perks and related tax-gross ups, certain features of change-in-control packages (excise tax gross-ups, single triggers, modified single triggers), multi-year guarantees for non-performance based bonuses, excessive pension benefits, option backdating, poor compensation disclosures, etc. The definition of pay-for-performance disconnect and the list of problematic pay practices have been refined over time and they continued to evolve after 2010 as ISS developed voting guidelines for newly mandated say on pay votes.

[§] If the board adopts a short-term pill without shareholder approval, ISS may recommend withholding the vote on a case-by-case basis (depending on rationale for adoption, date of adoption relative to next shareholder meeting, past record of accountability to shareholders, etc.).

to an existing poison pill without shareholder approval. Voting guideline (i) was put in place in 2003, while (ii) was adopted in 2005 (with substantial modifications in 2010)[**] and (iii) was added in 2010.

Board-level, other governance issues: ISS recommends withholding votes from the entire Board (except new nominees, that will be considered on a case-by-case basis) if: (i) problematic governance provisions are coupled with sustained poor stock performance relative to peers;[††] (ii) some directors attended less than 75% of the board and committee meetings and the firm fails to disclose their identity. Some version of voting guideline (i) was essentially in place for the entire sample period (2003-2010), but the definition of poor performance and poor governance has been refined over time. Guideline (ii) was adopted in 2007. Also, starting in 2008, ISS may recommend withholding votes from some/all directors up for election if the board is classified and a director who would otherwise receive a withhold recommendation for a board/committee level governance problem is not up for election.

Extraordinary circumstances: a final provision states that under extraordinary circumstances ISS may recommend withholding votes from directors individually, committee members or the entire board, due to (i) material failures of governance, stewardship or fiduciary responsibilities at the company, (ii) failure to replace management as appropriate; or (iii) egregious actions related to the director(s)' service on other boards that raise substantial doubt about their ability to effectively oversee management and serve the best interests of shareholder at any company. This provision was effectively in place for the entire 2003-2010 sample period (with slightly different language in some years), except for (iii), which was added in 2010.

Key changes after 2010[‡‡]

Committee-level (Compensation Committee): after the introduction of mandatory say on pay votes in 2011, compensation-related concerns are expressed through voting recommendation on say on pay proposals. However, if the say on pay proposal is opposed by more than 30% of the votes cast, ISS may recommend withholding the vote from the CC the subsequent year depending on a series of factors, especially how the board has responded to the concerns behind the say on pay vote.

Board responsiveness: starting in 2014, failure to act on a shareholder proposal that received approval by a majority of the shares cast the previous year is enough to trigger a withhold recommendation. However, the negative recommendation is no longer automatic but on a case-by-case basis, depending on a series of factors (e.g., the rationale given by the board, board engagement with investors, response to the vote, proposal topic and past history, voting support). Also ISS analysts are given some discretion as to whom to hold accountable (e.g., full board vs. nominating/governance committee). Commentators have predicted that this policy change will "shake up boards" (WSJ, 2013).

[**] ISS' poison pill policy for 2005-2009 was to recommend withholding votes from the entire Board if the board adopts or renews a poison pill without shareholder approval and without commitment to submit it to shareholder approval within 12 months of adoption.
[††] Examples of such provisions are a classified board, supermajority voting requirements, dual class structure, inability for shareholders to call special meetings or act by written consent, a non-shareholder approved poison pill and (after 2010), a lack of a majority voting standard for director elections.
[‡‡] Source: authors' summary based on ISS 2014 U.S. Proxy Voting Summary Guidelines.

Appendix 2: Computation of Estimated Rate of Responsiveness (Table 6)

Below we explain the criteria we used to estimate the rate of responsiveness reported in the last column of Table 6. As noted in the text, the lack of a repeated withhold from ISS may not necessarily mean that the firm was "responsive" (i.e., addressed the issue that caused the negative recommendation). Hence, we examine ISS reports in *t+1* to determine in each case whether the firm responded or not.

Individual Level – Independence:
> *Affiliated directors on AC (CC, NC):* classified as responsive if the director continues to be classified as affiliated but leaves the committee between years *t* and *t+1*; classified as not responsive if the director continues to be classified as affiliated but moves to another committee. If the director is no longer classified as affiliated, we classify it alternatively as responsive and not responsive (resulting in an estimated range in the last column of Table 6), since it is not clear whether it is the result of a responsive action that effectively eliminates the "affiliated" nature (e.g., director no longer works for a lender of the firm) or other factors (e.g., ISS changes definition of affiliated). We do not classify (as either responsive or not responsive) cases where the director is no longer affiliated because she has passed the "cooling off" period imposed by ISS (e.g., after a number of years a former executive is no longer considered affiliated)
> *Insider director on NC:* classified as responsive if the director is removed from the nominating committee.
> *Affiliated/Insider Directors – No Independent NC*: classified as responsive if the firm installs an independent NC. Classified as not responsive if the firm does not install an independent NC and the director receives a withhold recommendation in *t+1* for similar reasons (e.g., affiliated director is reclassified as insider in *t+1* or vice versa; director receives a withhold recommendation in *t+1* for general governance failure (of which the lack of independent nominating committee is one element).
> *Affiliated/Insider Directors – Board Not Independent*: classified as responsive if the board changed its independence structure by adding independent directors or replacing affiliated directors with independent directors. All the other cases involve an affiliated director who is no longer defined as affiliated in t+1, the reason is unclear (see earlier discussion). Hence, we classify them alternatively as responsive and not responsive (resulting in an estimated range in the last column of Table 6).

Individual Level – Attendance: classified as responsive if the director attends at least 75% the meetings during the subsequent year (this occurs in all the cases in our sample)

Individual Level – Busyness:
> *Individual Level - Busy: 3+Seats & CEO*: classified as responsive if the director either steps down from one or more boards or from the CEO position. However, we classify as not responsive cases where the director steps down from the CEO position (and, thus, does not receive a repeated withhold recommendation as *Busy: 3+Seats & CEO*) while holding

on to more than six board seats, resulting in a *Busy: 6+Seats* withhold recommendation in year *t+1*.

Individual Level – Busy: 6+Seats: classified as responsive if the director reduces the number of board memberships to below six. However, we classify as not responsive cases where the director additionally takes on a CEO position and receives a *Busy: 3+Seats & CEO* withhold recommendation in year *t+1*.

Committee Level

AC & NC Issues: classified as responsive if the firm addresses the underlying concern (all cases in our sample). The most common case in this category is a withhold recommendation for AC members due to excessive auditors' non-audit fees. All the firms receiving this recommendation reduced the auditors' non-audit fees by about 50%, with the new non-audit fees representing on average 30% of total auditors' fees (versus 60% before the negative recommendation).

Compensation Committee Issues – Pay for Performance: classified as responsive if the firm does not get a repeated withhold, since it means that the firm no longer fails the pay-for-performance test used by ISS. To validate the ISS assessment of responsiveness, we examine the change in CEO pay and find that after the year *t* negative recommendation these firms, on average, reduce CEO pay by 20% (while experiencing stock returns similar to their industry peers). In contrast, the three firms receiving a repeated withhold recommendation increase CEO pay by more than 10% while experiencing below-industry stock returns (and, thus, a worsening of the pay-performance relation, as measured by ISS).

Compensation Committee Issues – Poor Pay Practices: classified as responsive if, based on the ISS report at t+1, there is clear evidence that the firm addressed the problem identified in year *t*. We classify as not responsive cases where the firms does not address the problem, even if there is no repeated withhold (this may occur because of the ISS policy: e.g., ISS recommends a withhold from CC members in year *t* if a firm enters into a *new* employment agreement that provides for excise tax gross-ups, but does not recommend a withhold again the following year only because there is an excise tax gross-up in place in an existing agreement, unless more than 50% votes withheld were withheld from CC members in year *t*). We do not classify as either responsive or not responsive (and exclude from our computation) cases where the withhold recommendation is due to a specific transaction occurring in year *t* (e.g., a mega grant, some provision of an employment agreement, payments to an outgoing CEO) and that cannot be "undone" in year *t+1*. In these cases, it is not clear how the firm could have "responded" to the withhold recommendation, aside from avoiding similar behavior when presented with similar circumstances in the future.

Board Level

Lack of Responsiveness: classified as responsive if the firm implemented the shareholder proposal that won a majority of the shares outstanding the previous year or the majority of the votes cast vote in the previous two years. We classify as not responsive the cases where the firm has not implemented the proposal even if there is no repeated withhold in *t+1* (the reason for the lack of a repeated withhold in these cases is that the proposal was not represented at time *t*, hence there was not another vote at time *t*). We do not classify the few cases where we cannot determine whether the firm implemented the proposal or not.

Poison Pill: If the reason for the withhold recommendation is that the board approved a poison pill without shareholder approval (most of the cases in this category), we classify as responsive a firm that by *t+1* either terminates the poison pill or submits it to shareholder approval; we classify the firm as not responsive if the pill is still in place (without shareholder approval) at *t+1*. If the reason for the withhold recommendation is the presence of a poison pill with a "dead-hand" feature, we classify as responsive a firm that by *t+1* terminates the poison pill or removes that feature.

For the three sub-categories *Other Issues* in Table 6 (under Individual, Committee and Board Level), we classify as responsive cases where the firm addresses the concern underlying the recommendation and as not responsive the cases where no action is taken. We exclude from the computation of the rate of responsiveness cases where we cannot determine the firm's response.

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Table 1 Distribution of votes withheld conditional on proxy advisors' recommendations

	N (%)	Mean of *Votes Withheld*		Director-years with *Votes Withheld* between:			
				0 - 10%	**10 - 20%**	**20 - 50%**	**50 - 100%**
All Director-Year Observations	23,844 *100%*	5.0%	N %	21,312 *89.4%*	1,267 *5.3%*	1,247 *5.2%*	18 *0.1%*
with ISS Withhold Rec.	1,673 *7.0%*	24.7%	N %	185 *11.1%*	327 *19.5%*	1,143 *68.3%*	18 *1.1%*
without ISS Withhold Rec.	22,171 *93.0%*	3.6%	N %	21,127 *95.3%*	940 *4.2%*	104 *0.5%*	0 *0.0%*
with GL Withhold Rec.	3,275 *16.2%*	11.7%	N %	2,116 *64.6%*	584 *17.8%*	557 *17.0%*	18 *0.5%*
without GL Withhold Rec.	16,946 *83.8%*	3.7%	N %	15,993 *94.4%*	472 *2.8%*	481 *2.8%*	0 *0.0%*

Table 1 displays the distribution of observations and average votes withheld from directors for director-firm-years with and without Institutional Shareholder Services (ISS) and Glass, Lewis & Co. (GL) withhold recommendations. GL started providing recommendations in 2004. This results in a sample of 20,211 observations over the 2004 – 2010 period with GL recommendations. *Votes Withheld* is votes withheld from directors up for election as a fraction of votes cast (source: Voting Analytics).

Table 2 Determinants of votes withheld – role of proxy advisors' withhold recommendations

	Dependent Variable: Votes Withheld					
	Model 1: Benchmark		Model 2: Role of *ISS Withhold*		Model 3: Role of *ISS & GL Withhold*	
Variable	**Coeff.**	**t-statistic**	**Coeff.**	**t-statistic**	**Coeff.**	**t-statistic**
Intercept	-0.0236	-1.10	-0.0098	-0.64	-0.0136	-0.83
ISS Withhold			0.2062	24.53 ***	0.2077	27.13 ***
GL Withhold					0.0459	21.53 ***
Attend less than 75% of Meetings	0.1118	10.62 ***	0.0526	7.11 ***	0.0359	4.78 ***
New Director	-0.0099	-5.25 ***	-0.0037	-3.93 ***	-0.0012	-1.32
Independent Director	-0.0069	-2.65 ***	0.0040	1.47	0.0009	0.61
Linked Director	0.0302	7.92 ***	0.0140	4.92 ***	0.0038	1.72 *
Stock Ownership (%)	-0.0567	-3.46 ***	-0.0614	-2.42 **	-0.0280	-1.41
Tenure	0.0004	4.00 ***	0.0003	4.95 ***	0.0003	5.59 ***
Female Director	-0.0004	-0.40	-0.0011	-1.13	0.0002	0.26
Number of Other Directorships	0.0010	1.73 *	0.0011	3.08 ***	0.0001	0.20
Director Age > 65	0.0017	1.28	0.0004	0.43	-0.0007	-0.72
Compensation Committee Member	0.0209	11.95 ***	0.0092	8.22 ***	0.0055	5.23 ***
Audit Committee Member	0.0056	3.56 ***	0.0033	3.98 ***	0.0017	2.29 **
Other Committee Member	0.0062	4.50 ***	0.0008	0.98	0.0001	0.17
CEO	-0.0007	-0.31	0.0050	1.80 *	0.0055	3.82 ***
Entrenchment Index	0.0037	3.45 ***	0.0020	2.76 ***	0.0020	2.86 ***
Abnormal CEO Compensation	0.0005	3.74 ***	0.0002	1.31	0.0002	2.19 **
Board Size	-0.0005	-1.09	-0.0008	-2.37 **	-0.0004	-1.08
Board Holdings (%)	-0.0316	-3.20 ***	-0.0431	-4.38 ***	-0.0386	-3.61 ***
% of Outside Directors	-0.0174	-1.80 *	0.0121	1.51	0.0093	1.17
Restatement	0.0225	2.53 **	0.0138	1.99 **	0.0105	1.37
% of Institutional Holdings	0.0262	2.93 ***	0.0033	0.46	0.0043	0.58
ln(Assets)	0.0030	2.22 **	0.0010	1.02	0.0013	1.23
Industry Adjusted ROA	-0.0157	-0.96	-0.0219	-2.15 **	-0.0142	-1.47
Abnormal Returns	-0.0105	-3.50 ***	-0.0071	-3.45 ***	-0.0060	-2.95 ***
N	23,844		23,844		20,221	
Adjusted R^2	11.10%		64.10%		72.10%	

Table 2 presents the results for the determinants of votes withheld from directors at elections. The dependent variable, *Votes Withheld*, is votes withheld from directors up for election as a fraction of votes cast (source: Voting Analytics). *ISS* (*GL*)*Withhold* is an indicator variable that is equal to one if ISS (GL) recommends withholding votes from the director. *Attend less than 75% of Meetings* is an indicator variable that is equal to one for directors that attended less than 75% of meetings over the year (source: RiskMetrics Directors Dataset). *New Director* is an indicator variable that is equal to one if the director was not on board at the time of the prior annual meeting (source: RiskMetrics Directors Dataset). *Independent* (*Linked*) *Director* is an indicator variable that is equal to one if the director is deemed to be an

independent (gray) director (source: RiskMetrics Directors Dataset). *Stock Ownership (%)* is the percentage of shares owned by the director at the time of the annual meeting (source: RiskMetrics Directors Dataset). *Tenure* is the number of years the director has been on board (source: RiskMetrics Directors Dataset). *Female* is an indicator variable that is equal to one for female directors (source: RiskMetrics Directors Dataset). *Number of Other Directorships* is the number of other board seats the director holds in the RiskMetrics universe as of the time of the annual meeting (source: RiskMetrics Directors Dataset). *Director Age > 65* is an indicator variable that is equal to one if the director is older than 65 (source: RiskMetrics Directors Dataset). *Compensation (Audit, Other) Committee Member* is an indicator variable that is equal to one for directors who sit on the compensation (audit, other) committee (source: RiskMetrics Directors Dataset). *CEO* is an indicator variable that is equal to one if the director is the CEO of the firm (source: RiskMetrics Directors Dataset). All director characteristics are measured at the time of the annual meeting. *Entrenchment Index* counts how many of the following provisions are in place at the firm: chartered board, poison pill, golden parachute, requirement to approve merger, limited ability to amend charter and limits to amend bylaws (source: RiskMetrics Governance Dataset). *Abnormal CEO Compensation* is the difference between total CEO compensation for the most recent fiscal year prior to the annual meeting and predicted CEO pay, which, in turn is the exponent of the predicted value from a regression of the natural logarithm of total CEO compensation on proxies for economic determinants of CEO compensation (source: Execucomp, Compustat and CRSP). *Board Size* is the number of directors on the board at the time of the annual meeting (source: RiskMetrics Governance Dataset). *Board Holdings (%)* is the percentage of shares held by board members (source: RiskMetrics Governance Dataset). *% of Outside Directors* is the percentage of independent directors that are on the board (source: RiskMetrics Governance Dataset). *Restatement* is an indicator variable that is equal to one if the firm has an income-decreasing restatement in the 12-month period preceding the annual meeting (source: Audit Analytics). *% Institutional Holdings* is the percentage of equity owned by institutions based on 13-F filings (source: Thomson Reuters). *ln(Assets)* is the natural logarithm of total assets (Compustat data item *at*) as of the end of the fiscal year preceding annual meeting. *Industry Adjusted ROA* is the firm's return on assets (ROA) less average ROA for firms in the same two-digit SIC industry for the most recent fiscal year ending before the annual meeting. We calculate ROA as operating income before depreciation (Compustat data item o*ibdp*) scaled by average total assets (source: Compustat). *Abnormal Returns* is size-adjusted returns for the most recent fiscal year ending before the annual meeting (source: CRSP). We include year and industry fixed effects. ***, **, and * denote significance at the 0.01, 0.05, and 0.10 levels, respectively. Reported t-statistics are based on standard errors estimated using the Huber (1967)–White (1980) procedure, with director- and firm-level clustering (Rogers, 1993).

Table 3 Distribution of votes withheld conditional on ISS withhold rationale

| | 2003 – 2010 | | 2003 – 2006 | | 2007 – 2010 | | Directors with *Votes Withheld* between | | |
	N	Mean of *Votes Withheld*	N	Mean of *Votes Withheld*	N	Mean of *Votes Withheld*	**0 - 20%**	**20 - 50%**	**50 - 100%**
All ISS Withhold Recommendations	**1,762**	**24.67%**	**760**	**23.17%**	**1,002**	**25.91%**	**526**	**1,213**	**23**
Individual	**664**	**20.95%**	**414**	**20.50%**	**250**	**21.70%**	**301**	**360**	**3**
Independence	437	19.40%	295	19.93%	142	18.30%	207	229	1
Attendance	71	30.24%	41	27.86%	30	33.48%	12	59	0
Busyness	118	20.12%	69	18.31%	49	22.66%	69	47	2
Busy: 3+ Seats & CEO	103	18.62%	58	17.31%	45	21.50%	64	39	0
Busy: 6+ Seats	15	26.79%	11	23.55%	4	35.70%	5	8	2
Other	42	24.50%	13	24.40%	29	24.55%	13	29	0
Committee	**497**	**24.52%**	**72**	**19.72%**	**425**	**25.33%**	**139**	**355**	**3**
Audit & Nominating Committee	27	21.31%	18	20.99%	9	21.95%	13	14	0
Compensation Committee	473	24.63%	54	19.29%	419	25.31%	129	341	3
Pay for Performance Disconnect	119	23.05%	33	15.81%	86	25.83%	39	80	0
Poor Pay Practices	318	24.99%	11	25.17%	307	24.98%	85	230	3
Other	65	29.15%	15	25.28%	50	30.31%	5	60	0
Board	**580**	**29.70%**	**295**	**27.96%**	**285**	**31.49%**	**83**	**483**	**14**
Lack of Responsiveness	419	29.79%	222	27.71%	197	32.13%	50	356	13
Poison Pill	95	32.85%	65	29.55%	30	40.01%	10	81	4
Other	80	26.53%	15	23.40%	65	27.25%	23	57	0

Table 3 presents the distribution of observations and average votes withheld from directors for the subset of 1,762 observations with ISS withhold recommendations conditional on the rationale for the withhold recommendation. We partition director-firm-years into three broad categories depending on whether the withhold recommendation is issued for an individual director (*Individual)*, for every director that is a member of a specific committee (*Committee)* or for every member of the board (*Board)*. Within each category, we further group observations to finer sub-categories.

Table 4 Determinants of votes withheld – role of ISS withhold recommendation rationale and firm characteristics

	Dependent Variable: Votes Withheld							
	Model 1:		Model 2:		Model 3:		Model 4:	
	Single versus multiple withhold reasons		Individual-, committee- and board-level issues partition		Above/below median e-index		Excess comp. split	
Variable	**Coeff.**	**t-statistic**	**Coeff.**	**t-statistic**	**Coeff.**	**t-statistic**	**Coeff.**	**t-statistic**
ISS Withhold–Single Reason	0.2047	24.34 ***						
ISS Withhold–Multiple Reasons	0.2526	13.47 ***	0.2509	13.06 ***				
ISS Withhold–Single Reason–Individual			0.1644	14.65 ***				
ISS Withhold–Single Reason–Committee			0.1973	25.28 ***				
ISS Withhold–Single Reason–Board			0.2548	19.70 ***				
ISS Withhold–Below Median E-Index					0.1684	12.84 ***		
ISS Withhold–Above Median E-Index					0.2224	26.47 ***		
ISS Withhold–Negative Excess Comp							0.1916	22.36 ***
ISS Withhold–Positive Excess Comp							0.2149	22.00 ***
Control Variables	Included		Included		Included		Included	
N	23,844		23,844		23,844		23,844	
Adjusted R^2	64.10%		66.00%		65.30%		64.70%	

	Model 1:		Model 2:		Model 3:		Model 4:	
Wald tests	**Coeff.**	**χ^2**	**Coeff.**	**χ^2**	**Coeff.**	**χ^2**	**Coeff.**	**χ^2**
Single versus *Multiple Reasons*	-0.0479	6.91 ***						
Single Reason–Individual versus *Committee*			-0.0329	6.64 ***				
Single Reason–Individual versus *Board*			-0.0904	28.88 ***				
Single Reason–Committee versus *Board*			-0.0575	14.19 ***				
Above vs. *Below Median E-Index*					0.0540	14.29 ***		
Positive vs. *Negative Excess Comp*							0.0233	2.85 *

Table 4 presents the results for the determinants of votes withheld from directors at elections depending on the severity of the recommendation. The dependent variable, *Votes Withheld*, is votes withheld from directors up for election as a fraction of votes cast (source: Voting Analytics). *ISS Withhold–Single Reason* (*Multiple Reasons*) is an indicator variable that is equal to one if ISS recommends withholding votes from the director based on a single (multiple) reason(s). For directors who receive a withhold recommendation because of a single reason, we construct a series of indicator variables that capture the categories and sub-categories of withhold reasons in Table 3. *ISS Withhold–Single Reason–Individual* (*Committee*, *Board*) is an indicator variable that is equal to one for directors who receive a withhold recommendation for an individual-level (committee-level, board-level) concern. *ISS Withhold–Below* (*Above*) *Median E-Index* is an indicator variable that is equal to one if the director receives an ISS withhold recommendation at a firm with below (above) median entrenchment index. *ISS Withhold–Negative* (*Positive*) *Excess Comp* is an indicator variable that is equal to one if the director receives an ISS withhold recommendation at a firm with negative (positive) *Abnormal CEO Compensation*. We include the same set of control variables as in Table 2 but suppress them for expositional reasons. We include year and industry fixed effects. ***, **, and * denote significance at the 0.01, 0.05, and 0.10 levels, respectively. Reported t-statistics are based on standard errors estimated using the Huber (1967)–White (1980) procedure, with director- and firm-level clustering (Rogers, 1993).

Table 5 Votes withheld from directors and subsequent director turnover

	Model 1 Coeff.	t-statistic		Model 2 Coeff.	t-statistic		Model 3 Coeff.	t-statistic		Model 4 Coeff.	t-statistic	
						Dependent Variable: Director Turnover						
Intercept	-2.7100	-7.19	***	-2.6930	-7.13	***	-2.7100	-7.12	***	-2.7010	-7.13	***
Votes Withheld	0.7720	1.79	*									
Votes Withheld >= 20%				0.1840	1.61							
Votes Withheld >= 50%							0.8890	1.15				
Votes Withheld >= 20%–No ISS Withhold Rec.										0.1510	0.51	
Votes Withheld >= 20%–Single Reason–Individual										0.2930	1.28	
Votes Withheld >= 20%–Single Reason–Committee										-0.1680	-0.73	
Votes Withheld >= 20%–Single Reason–Board										0.1810	0.85	
Votes Withheld >= 20%–Multiple Reasons										0.5480	1.14	
Attend less than 75% of Meetings	0.7090	3.01	***	0.7430	3.21	***	0.7960	3.46	***	0.6990	2.92	***
New Director	-0.5100	-4.53	***	-0.5140	-4.57	***	-0.5190	-4.62	***	-0.5150	-4.57	***
Independent Director	-0.8420	-6.78	***	-0.8440	-6.78	***	-0.8490	-6.83	***	-0.8370	-6.71	***
Linked Director	-0.5040	-3.66	***	-0.4960	-3.63	***	-0.4830	-3.56	***	-0.5080	-3.66	***
Stock Ownership (%)	-6.5700	-2.39	**	-6.5960	-2.39	**	-6.5990	-2.39	**	-6.5960	-2.39	**
Tenure	0.0200	4.74	***	0.0200	4.78	***	0.0200	4.77	***	0.0200	4.80	***
Female Director	-0.0920	-1.21		-0.0920	-1.20		-0.0910	-1.19		-0.0920	-1.20	
Number of Other Directorships	-0.0310	-0.97		-0.0300	-0.93		-0.0300	-0.93		-0.0310	-0.96	
Director Age > 65	0.6170	9.64	***	0.6170	9.65	***	0.6180	9.66	***	0.6160	9.64	***
Compensation Committee Member	-0.0940	-1.42		-0.0870	-1.32		-0.0760	-1.17		-0.0800	-1.22	
Audit Committee Member	-0.2230	-3.66	***	-0.2210	-3.62	***	-0.2170	-3.56	***	-0.2230	-3.64	***
Other Committee Member	-0.1350	-2.42	**	-0.1320	-2.37	**	-0.1280	-2.32	**	-0.1370	-2.43	**
CEO	-0.8990	-7.00	***	-0.9000	-7.01	***	-0.8990	-6.99	***	-0.8990	-6.99	***
Entrenchment Index	0.0070	0.20		0.0080	0.22		0.0070	0.21		0.0060	0.18	
Classified Board	-0.3700	-3.83	***	-0.3670	-3.79	***	-0.3610	-3.73	***	-0.3640	-3.77	***
Abnormal CEO Compensation	-0.0050	-1.32		-0.0050	-1.29		-0.0040	-1.23		-0.0040	-1.22	
Board Size	0.0380	2.27	**	0.0370	2.23	**	0.0370	2.23	**	0.0370	2.24	**
Board Holdings (%)	-0.0520	-0.14		-0.0700	-0.20		-0.0820	-0.23		-0.0650	-0.18	
% of Outside Directors	0.2870	0.84		0.2800	0.82		0.2780	0.81		0.2750	0.80	
Restatement	0.0810	0.50		0.0920	0.57		0.1020	0.64		0.1020	0.63	
CEO Turnover	0.5300	7.75	***	0.5320	7.78	***	0.5310	7.75	***	0.5310	7.78	***
Change in Institutional Holdings	0.0860	0.21		0.0930	0.23		0.1090	0.27		0.1000	0.25	
ln(Assets)	0.1030	2.97	***	0.1030	2.96	***	0.1050	2.98	***	0.1030	2.96	***
Industry Adjusted ROA	0.2600	0.23		0.2560	0.23		0.2800	0.25		0.2850	0.25	
Industry Adjusted ROA–Subsequent to Meeting	-1.3630	-1.28		-1.3830	-1.30		-1.4010	-1.32		-1.4070	-1.33	
Abnormal Returns	-0.2670	-1.89	*	-0.2700	-1.90	*	-0.2750	-1.94	*	-0.2780	-1.98	**
Abnormal Returns–Subsequent to Meeting	-0.1150	-0.80		-0.1180	-0.82		-0.1210	-0.84		-0.1160	-0.81	
N	22,458			22,458			22,458			22,458		
N(Director Turnover = 1)	1,829			1,829			1,829			1,829		
Pseudo R^2	6.16%			6.16%			6.15%			6.18%		

Table 5 presents the results for the analysis of the relation between votes withheld from directors at annual elections and director turnover for the 22,471 observations in our sample for which we are able to determine director turnover. The dependent variable, *Director Turnover*, is an indicator variable that is equal to one if the director loses his/her seat between the annual meeting in year *t* and the annual meeting in year *t+1* (source: RiskMetrics Directors Dataset). *Votes Withheld*, is votes withheld from directors up for election as a fraction of votes cast (source: Voting Analytics). *Votes Withheld >= 20%* (*50%*) is an indicator variable that is equal to one if the percentage of votes withheld from the director is greater than or equal to 20% (50%). *Votes Withheld >= 20%–No ISS Withhold Rec.* is an indicator variable that is equal to one if the percentage of votes withheld from the director is greater than or equal to 20% and the director did not receive a withhold recommendation from ISS. *Votes Withheld >= 20%–Single Reason–Individual* (*Committee*, *Board*) is an indicator variable that is equal to one if the percentage of votes withheld from the director is greater than or equal to 20% and the director received a single-reason individual-level (committee-level, board-level) withhold recommendation from ISS. *Votes Withheld >= 20%–Multiple Reasons* is an indicator variable that is equal to one if the percentage of votes withheld from the director is greater than or equal to 20% and the director received a multiple-reason withhold recommendation from ISS. *Classified Board* is an indicator variable that is equal to one if the firm has a classified board structure at the time of the year *t* annual meeting (source: RiskMetrics). *CEO Turnover* is an indicator variable that is equal to one if the CEO of the firm turns over during the fiscal year preceding annual meeting in year *t+1* (source: Execucomp). *Industry Adjusted ROA–Subsequent to Meeting* is the firm's return on assets (ROA) less average ROA for firms in the same two-digit SIC industry for the most recent fiscal year ending before the *t+1* annual meeting. *Abnormal Returns–Subsequent to Meeting* is size-adjusted returns for the most recent fiscal year ending before the *t+1* annual meeting (source: CRSP). All other variables are defined as in Table 2. We include year and industry fixed effects. ***, **, and * denote significance at the 0.01, 0.05, and 0.10 levels, respectively. Reported t-statistics are based on standard errors estimated using the Huber (1967)–White (1980) procedure, with director- and firm-level clustering (Rogers, 1993).

Table 6 Firms' responsiveness to ISS recommendations to withhold votes from directors

	# of observations with withheld rec. at year t (# of firm-years)	# of observations where year $t+1$ withhold rec. and rationale observable	# observations without withhold rec. (same reason) at year $t+1$	% observations without withhold rec. (same reason) at year $t+1$	Estimated Rate of Responsiveness
Individual Level					**32.1 – 45.2%**
Independence					
Affiliated Director on AC	96	58	30	51.7%	14.0 – 40.0%
Affiliated Director on CC	123	78	42	53.8%	17.8 – 47.9%
Affiliated Director on NC	201	129	67	51.9%	20.0 – 47.2%
Insider Director on NC	19	12	4	33.3%	33.3%
Affiliated/Insider Director–No Independent NC	74	59	25	42.4%	27.1%
Affiliated/Insider Director–Board not Independent	108	84	35	41.7%	27.4 – 41.7%
Attendance	71	41	41	100.0%	100.0%
Busyness					
Busy: 3+ Seats & CEO	103	69	30	43.5%	40.6%
Busy: 6+ Seats	15	8	8	100.0%	75.0%
Other	42	15	15	100.0%	50.0%
Committee Level					**60.1%**
Audit & Nominating Committee Issues	27 (12)	12	12	100.0%	100.0%
Compensation Committee Issues					
Pay & Performance Disconnect	119 (40)	40	37	92.5%	92.5%
Poor Pay Practices	318 (107)	104	81	77.9%	56.9%
Other	65 (20)	20	16	80.0%	46.2%
Board Level					**42.2%**
Lack of Responsiveness	419 (93)	92	68	73.9%	48.9%
Poison Pill	95 (19)	19	17	89.5%	15.8%
Other	80 (13)	12	9	75.0%	33.3%
Total					**39.0 –47.7%**

Table 6 provides an estimate of the rate of responsiveness to ISS withhold recommendations. The first column reports the distribution of ISS withhold recommendations over our sample period, similar to Table 3 (but with a more granular description of certain categories). The second column reports the subset of observations with available information on the ISS recommendations and their rationale in year $t+1$ (attrition due to turnover and classified boards in the case of

individual-level recommendations, and mergers or delistings in the other cases). The third (fourth) column reports the number (percentage) of cases where the withhold recommendation in year t is not repeated in year $t+1$ (upper bound estimate of the rate of responsiveness to the year t withhold recommendation). The last column provides our estimate of the rate of responsiveness to ISS withhold recommendations in year t. based on the director and firm actions described in the $t+1$ ISS report (see Section 4.2 and Appendix 2 for details).

Table 7 Recommendations to withhold votes from directors and subsequent turnover on key committees

	Dependent Variable: NC Turnover		Dependent Variable: CC Turnover		Dependent Variable: AC Turnover	
	Model 1		Model 2		Model 3	
	Coeff.	**t-statistic**	**Coeff.**	**t-statistic**	**Coeff.**	**t-statistic**
Intercept	-13.1460	-9.86 ***	-13.0910	-11.22 ***	-12.1980	-10.69 ***
ISS Withhold–Independence	0.9810	4.21 ***	0.8350	2.61 ***	0.9560	3.02 ***
ISS Withhold–Non-Independence	-0.1710	-0.95	-0.0240	-0.14	-0.1440	-0.76
Attend less than 75% of Meetings	-0.6780	-1.06	-0.4370	-0.81	-0.1820	-0.33
New Director	-0.1190	-0.58	-0.5620	-2.50 **	-0.7330	-4.01 ***
Stock Ownership (%)	0.7440	0.39	-0.3240	-0.13	-9.5110	-0.89
Tenure	0.0070	1.09	0.0090	1.27	0.0120	1.79 *
Female Director	-0.3390	-2.79 ***	-0.2020	-1.60	-0.2410	-2.34 **
Number of Other Directorships	-0.0140	-0.33	0.0200	0.46	0.0800	2.14 **
Director Age > 65	-0.0090	-0.10	0.1700	1.86 *	-0.3320	-3.51 ***
Number of Committees	-0.0460	-0.56	-0.1520	-2.20 **	0.0180	0.28
% of Institutional Holdings	-0.4740	-1.14	-0.1580	-0.43	-0.2130	-0.62
Blockholder	0.0860	0.61	0.0470	0.39	-0.1310	-1.29
ln(Assets)	-0.0260	-0.51	0.0230	0.51	-0.0730	-1.82 *
Industry Adjusted ROA	-0.9760	-1.39	-0.8950	-1.47	-0.5030	-0.98
Abnormal Returns	-0.1930	-1.13	-0.1170	-0.71	-0.0640	-0.46
N	7,930		7,357		7,786	
N(*Committee Turnover* = 1)	782		753		807	
Pseudo R^2	14.32%		12.82%		11.72%	

Table 7 presents the results for the analysis of the relation between ISS withhold recommendations/votes withheld from directors at annual elections and nominating, compensation and audit committee turnover. Each sample is limited to directors who sit on the respective committee at the year t meeting and are still on the board at the time of the year $t+1$ annual meeting. The dependent variable, *NC* (*CC*, *AC*) *Turnover*, is an indicator variable that is equal to one if the director sits on the nominating (compensation, audit) committee at the year t meeting, remains on the board but is no longer on the nominating (compensation, audit) committee at year $t+1$. *NC* (*CC, AC*) *Turnover* is equal to zero if the director remains on the respective committee at year $t+1$ meeting. In Model 1 (Model

2, Model 3) *ISS Withhold Rec.–Independence* is an indicator variable that is equal to one if a director on the nominating (compensation, audit) committee receives an independence-related ISS withhold recommendation. *ISS Withhold–Non-Independence* is an indicator variable that is equal to one if the director receives a non-independent related withhold recommendation from ISS. *Blockholder* is an indicator variable that is equal to one if the firm has at least one institutional investor with at least 5% ownership. All other variables are defined as in Table 2. We include year and industry fixed effects. [***], [**], and [*] denote significance at the 0.01, 0.05, and 0.10 levels, respectively. Reported t-statistics are based on standard errors estimated using the Huber (1967)–White (1980) procedure, with director- and firm-level clustering (Rogers, 1993).

Table 8 Recommendations to withhold votes from directors and subsequent change in abnormal CEO compensation

	*Dependent Variable: Change in CEO % Residual Pay*							
	Model 1		Model 2		Model 3		Model 4	
	Coefficient	**t-statistic**	**Coefficient**	**t-statistic**	**Coefficient**	**t-statistic**	**Coefficient**	**t-statistic**
Intercept	0.0074	1.00	0.0084	1.14	0.0528	4.25 ***	0.0599	4.43 ***
ISS Withhold–Compensation	-0.1616	-3.01 ***						
Pay-for-Performance			-0.3596	-3.52 ***	-0.1762	-2.10 **	-0.1791	-2.13 **
Poor Pay Practices			-0.1310	-2.06 **	0.0207	0.35	0.0239	0.40
Other			-0.0202	-0.17	0.1049	0.76	0.1166	0.84
ISS Withhold–Non-Compensation							-0.0073	-0.27
Shareholder Proposal–Compensation							-0.0822	-1.55
Votes For–Shareholder Proposal–Compensation							0.1344	1.02
Lag CEO % Residual Pay					-0.4890	-15.54 ***	-0.4894	-15.46 ***
N	3,335		3,335		3,335		3,335	
Adjusted R^2	0.30%		0.50%		28.60%		28.50%	

Table 8 presents the results for the analysis of the relation between ISS withhold recommendations from directors at annual elections and subsequent change in abnormal CEO compensation. The dependent variable, *Change in CEO % Residual Pay* is the difference between *CEO % Residual Pay* for year *t+1* and year *t*. *CEO % Residual Pay* is defined as the natural logarithm of *CEO Total Pay* less the natural logarithm of *CEO Predicted Pay*. Therefore, *Change in CEO % Residual Pay* captures the change in percentage excess CEO pay between years *t+1* and *t*. *ISS Withhold–Compensation* is an indicator variable that is equal to one if there is at least one compensation-related withhold recommendation at year *t* annual meeting. *Pay-for-Performance* (*Poor Pay Practices*, *Other*) is an indicator variable that is equal to one if there is at least one compensation-related withhold recommendation that pertains to pay-for-performance issues (poor pay practices, other compensation-related issues) at the year *t* annual meeting. *ISS Withhold–Non-Compensation*, is an indicator variable that is equal to one if there is at least one non-compensation-related withhold recommendation at the year *t* annual meeting. *Shareholder Proposal–Compensation* is an indicator variable that is equal to one if there is at least one compensation-related shareholder proposal voted upon at the year *t* annual meeting. *Votes For– Shareholder Proposal– Compensation* is the average percentage of votes cast in favor of compensation-related shareholder proposals voted upon at the annual meeting. *Votes For– Shareholder Proposal–Compensation* equals zero for firms without a compensation related shareholder proposal on the ballot. *Lag CEO % Residual Pay* is the *CEO % Residual Pay* for year *t*. ***, **, and * denote significance at the 0.01, 0.05, and 0.10 levels, respectively. Reported t-statistics are based on standard errors estimated using the Huber (1967)–White (1980) procedure, with firm-level clustering (Rogers, 1993).

Table 9 Recommendations to withhold votes from directors and probability of declassifying the board in the subsequent year

| | Dependent Variable = *Remove Classified Board* | | | | |
| | Model 1: | | | Model 2: | |
	Coefficient	**t-statistic**		**Coefficient**	**t-statistic**
Intercept	-3.3836	-19.48 ***		-3.4821	-5.28 ***
ISS Withhold–Failure to Declassify	2.3670	4.98 ***		2.4251	5.27 ***
ISS Withhold–All Other	0.7983	1.86 *		0.8408	2.20 **
% of Outside Directors				0.3695	0.45
Board Holdings (%)				-1.8321	-1.03
Industry Adjusted ROA				-2.1739	-2.44 **
Abnormal Returns				-0.4669	-2.83 ***
N	1,310			1,310	
N (*Remove Classified Board* = 1)	107			107	
Pseudo R^2	9.77%			10.77%	
	Model 1:			Model 2:	
Wald Tests	**Coeff.**	χ^2		**Coeff.**	χ^2
ISS Withhold–Failure to Declassify vs. *ISS Withhold–Other*	1.5687	6.90 ***		1.5843	7.91 ***

Table 9 presents the results for the role of ISS withhold recommendations that stem from firms' failure to declassify the board in response to shareholder proposals that receive majority voting support. In both models, we limit the sample to firms with a classified board in place at the time of the year *t* annual meeting and that do not receive a majority-vote shareholder proposal to declassify the board at the year *t* annual meeting. The dependent variable, *Remove Classified Board*, is an indicator variable that is equal to one if the firm removes the classified board between the year *t* and *t+1* annual meetings. *ISS Withhold–Failure to Declassify* is an indicator variable that is equal to one if the firm receives an ISS withhold recommendation for lack of responsiveness to majority-vote shareholder proposals to declassify the board. *ISS Withhold–All Other* is an indicator variable that is equal to one if the firm receives an ISS withhold recommendation for any other reason. All other variables are defined as in Table 2. We include year fixed effects in the estimation. ***, **, and * denote significance at the 0.01, 0.05, and 0.10 levels, respectively. Reported t-statistics are based on standard errors estimated using the Huber (1967)–White (1980) procedure, with firm-level clustering (Rogers, 1993).

Table 10 Firms' responsiveness: determinants and performance consequences

Panel A Determinants of firms' responsiveness

	Dependent Variable: Responsive					
	Model 1		Model 2		Model 3	
	Coeff.	**t-statistic**	**Coeff.**	**t-statistic**	**Coeff.**	**t-statistic**
Intercept	1.1696	0.93	1.2621	0.94	0.9333	0.71
Max Votes Withheld	2.8101	2.67 ***			2.6341	2.51 **
Multiple Withholds			0.4935	1.98 **	0.4281	1.69 *
% of Outside Directors	0.3554	0.46	1.1309	1.31	0.8284	1.00
Stock Ownership (%)	-0.9029	-1.03	-1.6000	-1.73 *	-0.9728	-1.09
% of Institutional Holdings	-1.3570	-1.66 *	-1.0906	-1.28	-1.4192	-1.68 *
ln(Assets)	-0.0171	-0.20	-0.0524	-0.56	-0.0363	-0.39
Industry Adjusted ROA	-3.1196	-2.01 **	-3.0902	-2.06 **	-3.0917	-2.03 **
Abnormal Returns–Pre	-0.5451	-2.00 **	-0.5918	-2.17 **	-0.5603	-2.07 **
N	481		481		481	
Pseudo R^2	6.25%		5.57%		6.75%	

Panel B Performance consequences of firm's responsiveness

	Dependent Variable: Change in Industry Adjusted ROA		*Dependent Variable: Change in Industry Adjusted Tobin's Q*		*Dependent Variable: Abnormal Returns–Post*	
	Model 1		Model 2		Model 3	
	Coeff.	**t-statistic**	**Coeff.**	**t-statistic**	**Coeff.**	**t-statistic**
Intercept	0.0266	6.17 ***	0.0184	6.28 ***	0.0918	2.23 **
Responsive	-0.0025	-0.83	-0.0015	-0.82	-0.0112	-0.41
Industry Adjusted ROA	-0.1634	-5.32 ***				
Tobin's Q			-0.0627	-3.53 ***		
Abnormal Return–Pre					-0.0240	-0.44
N	481		481		481	
Pseudo R^2	19.50%		12.70%		0.89%	

Table 10 presents the results for the determinants of firms' responsiveness (Panel A) and the association between responsiveness and change in performance (Panel B). We limit the sample to firm-years with at least one withhold recommendation for which we can assess responsiveness. In Panel A the dependent variable, *Responsive*, is an indicator variable if the firm is responsive to at least one withhold recommendation, and zero otherwise. *Max Votes Withheld* is the maximum votes withheld from directors for a given firm-year observation. *Multiple Withholds* is an indicator variable that is equal to one if the firm receives at least one other withhold recommendation from ISS. *Abnormal Returns–Pre* is size-adjusted returns for the 12-month period before the annual meeting (source: CRSP). The dependent variable in Panel B, Model 1, *Change in Industry Adjusted ROA* (*Change in Industry Adjusted Tobin's Q*), is the change in *Industry Adjusted ROA* (*Change in Industry Adjusted Tobin's Q*) surrounding the annual meeting where the firm is targeted. *Abnormal Returns–Post* is size-adjusted returns for the 12-month period subsequent to the annual meeting (source: CRSP). We calculate *Tobin's Q* as market value of equity (Compustat item *prcc_f* multiplied by Compustat item *csho*) plus book value of assets adjusted for deferred taxes (Compustat item *at* less Compustat item *ceq* less Compustat item *txdb*) scaled by total assets (Compustat item *at*). For industry adjustment we calculate industry median Tobin's Q for the 48 Fama-French industries. All other variables are defined as in Table 2. We include year fixed effects in the estimation. ***, **, and * denote significance at the 0.01, 0.05, and 0.10 levels, respectively. Reported t-statistics are based on standard errors estimated using the Huber (1967)–White (1980) procedure, with firm-level clustering (Rogers, 1993).