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ARTICLES

DIRECTOR ELECTIONS AND THE ROLE OF PROXY ADVISORS

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ABSTRACT

Using a dataset of proxy recommendations and voting results for uncontested director elections from 2005 and 2006 at Standard & Poor's 1500 companies, we examine how advisors make their recommendations. Of the four firms we study—Institutional Shareholder Services (“ISS”), PROXY Governance, Inc. (“PG”), Glass, Lewis & Company (“GL”), and Egan-Jones Proxy (“EJ”)—ISS has the largest market share and is widely regarded as the most influential. We find that the four proxy advisory firms differ substantially from each other in their willingness to issue a withhold recommendation, in the factors that affect their recommendations, and in the relative weight of those factors. Specifically, ISS focuses on governance-related factors, PG on compensation-related factors, GL on audit/disclosure-related factors, and EJ on an eclectic mix of factors. To the extent these differences are understood, institutional investors can subscribe to those advisors whose recommendations best conform to the

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The authors thank Glass Lewis, PROXY Governance, and Egan-Jones for access to their voting recommendations and policies. We would also like to thank, for their helpful comments, Cindy Alexander, Martijn Cremers, Robert Daines, Un Kyung Park, Roberta Romano, Randall Thomas, and participants at faculty workshops at the New York University School of Law, Columbia Law School, Vanderbilt Law School, and Harvard Law School.

investors' assessments of value-maximizing corporate governance. But if these differences are not known, then proxy advisors may lack accountability for—and can pursue their own agenda in making—their voting recommendations, thereby impairing the effectiveness of the shareholder franchise.

I. INTRODUCTION

Proxy advisory firms provide services to investors in connection with shareholder voting. Proxy advisory services had their start in the mid-1980s, when Institutional Shareholder Services (“ISS”), now a business unit of RiskMetrics Group, was founded. More recently, several other firms—notably, PROXY Governance, Inc. (“PG”), Glass, Lewis & Company (“GL”), and Egan-Jones Proxy (“EJ”)—have started to offer proxy advice. These firms, which typically operate on a subscription basis, research proxy issues, issue voting recommendations, and assist institutional investors in formulating voting guidelines.

Critics have expressed concerns about the influence that proxy advisors in general, and ISS in particular, can potentially exert over the shareholder voting process. Proxy advisors are depicted as powerful, yet unaccountable, institutions that can sway the outcome of corporate votes without any of their own money at stake. In addition to concerns about this extreme level of influence, commentators have identified potential conflicts of interest that might compromise the integrity of voting recommendations. These concerns are intensified by the limited transparency that proxy advisors provide about the processes by which their recommendations are determined. This lack of transparency has led the U.S. Chamber of Commerce to describe ISS’s process for making proxy recommendations as a “black box.”¹

Because institutional investors now have the ability to choose among several different proxy advisors, the extent to which the advisors’ policy determinations are transparent becomes an important factor in ascertaining the efficiency of the market for proxy advisory services. The efficiency of this market has the potential to affect critically the outcomes of corporate elections. Numerous developments, including recent calls for increased shareholder activism, regulatory reforms that increase institutional investor obligations to vote responsibly, attempts to expand shareholder voting rights (via proxy access and “say on pay” initiatives), and the move from

1. Rachel McTague, *Chamber Approaches RiskMetrics with Proposed Changes to Policy-Setting*, 40 Sec. Reg. & L. Rep. (BNA) 569, 589 (2008).

plurality to majority voting in director elections, all increase the potential importance of the shareholder franchise and thereby increase the potential effect of the proxy advisory firms that influence the manner in which shareholders vote. If institutional investors understand the basis for voting recommendations of the various proxy advisors, they can subscribe to and follow the recommendations of those advisors that best match their assessment of which votes maximize corporate value. On the other hand, if institutional investors lack such understanding and choose to follow a proxy advisor based on other criteria, then proxy advisors are indeed, as charged by their critics, powerful, unaccountable, badly incentivized, and able to pursue their own agenda in issuing voting recommendations.

In light of these concerns, understanding the role and influence of proxy advisors is critically important. Using a dataset of director elections at Standard & Poor's ("S&P") 1500 companies and proxy recommendations for 2005 and 2006, this Article examines the factors that affect the recommendations made by the four major proxy advisory firms—ISS, PG, GL, and EJ—in uncontested director elections. It is the first article to examine empirically the factors that affect these voting recommendations and the first article that compares the recommendations made by several proxy advisors.

The Article proceeds as follows: Part II describes the development of the market for proxy advisory services, the main proxy advisory firms, and the institutional context in which those firms operate. Part III describes our basic regression analysis in which we analyze the relationship between withhold recommendations and a variety of director-specific, firm, and market factors that might be expected to influence the likelihood of a withhold recommendation. Part IV presents an interaction analysis in which we examine the relationship between several key factors. Part V examines whether directors who receive nominations for multiple boards receive different recommendations compared with directors who sit on only one board. Part VI discusses how group-based and spillover effects might influence whether advisory firms issue withhold recommendations. Part VII considers the implications of our findings.

II. THE EVOLUTION OF PROXY ADVISORS AND THEIR SERVICES

ISS, the first proxy advisor, was founded in 1985 and began to provide

proxy advisory services to institutional investor clients in 1986.² ISS provides these services on a subscription basis. A subscription entitles the client to ISS's voting recommendations as well as a report detailing the underlying research and analysis upon which those recommendations are based.³ Additionally, ISS offers assistance in developing the client's voting guidelines, providing issuer-specific research, and handling the mechanical process of voting the client's shares.⁴ Clients may delegate to ISS the authority to vote their proxies, either in accordance with the client's own voting guidelines or in accordance with ISS recommendations.⁵ ISS also evaluates issuer corporate governance and releases highly publicized corporate governance ratings in which issuers are scored based on their corporate governance structure and policies.⁶

For many years, ISS faced a competitor—Proxy Monitor—that offered similar services, including voting recommendations.⁷ In 2001, however, the two companies effectively merged when Proxy Monitor acquired ISS.⁸ The merger left ISS as the sole proxy advisor and created a monopoly.⁹ Today, ISS remains the dominant proxy advisory firm. According to Robert Daines, Ian Gow, and David Larcker, "ISS claims over 1,700 institutional clients managing \$26 trillion in assets, including 24 of the top 25 mutual funds, 25 of the top 25 asset managers and 17 of the

2. RiskMetrics Group, Company History, <http://www.riskmetrics.com/history> (last visited Apr. 20, 2009).

3. RISKMETRICS GROUP, PROXY RESEARCH SERVICES FOR INSTITUTIONAL INVESTORS WORLDWIDE 1–3 (2009), available at <http://www.riskmetrics.com/sites/default/files/GS1-Proxy%20Research%20Services.pdf>. ISS recommendations are frequently reported in the media. See, e.g., John D. Stoll & Stephen Wisniewski, *ISS Recommends Lear Holders Reject Icahn Bid*, WALL ST. J., June 21, 2007, at A12 (reporting ISS's recommendation against Carl Icahn's proposed takeover of Lear).

4. RISKMETRICS GROUP, *supra* note 3, at 1–3.

5. *Id.* at 2. Some companies have made notable use of these proxy voting services. See, e.g., Luisa Beltran, *ISS Could Kill HP-Compaq*, CNNMONEY, Mar. 4, 2002, http://money.cnn.com/2002/03/04/deals/iss_hp/index.htm (describing how Barclays Global Investors delegated to ISS the authority to vote its nearly sixty million Hewlett-Packard shares in the vote on the merger with Compaq Computer Corporation and how one Barclays spokesman stated "[w]e provided ISS the authority to vote the shares" and "[w]e have no influence on how they are going to vote").

6. Robert Daines, Ian Gow & David Larcker, *Rating the Ratings: How Good Are Commercial Governance Ratings?* 8–10 (Stanford Univ. Rock Ctr. for Corp. Governance Working Paper Series, Paper No. 1, 2008), available at <http://ssrn.com/abstract=1152093>. Firms are given a score based on their standing within their own industry and a score based on their standing within their index (for example, Microsoft standing within the S&P 500). *Id.* at 9.

7. See *Investor Group Acquires Stake in Proxy Monitor*, WALL ST. J., June 10, 1998, at A8.

8. Mark Thomsen, *Proxy Monitor Buys ISS*, SOCIALFUNDS, Aug. 13, 2001, <http://www.socialfunds.com/news/article.cgi/648.html>.

9. Martha McNeil Hamilton, *Player in the Proxy Wars: HP-Compaq Merger Has Brought a Shareholder-Services Firm out of Obscurity*, WASH. POST, Apr. 1, 2002, at E01 (describing ISS as "something close to a monopoly").

top 25 public pension funds.”¹⁰ In 2006, ISS was acquired by RiskMetrics Group, a publicly traded company specializing in risk management services.¹¹

In addition to serving investors, ISS provides governance consulting to corporate issuers. For issuers, ISS offers “advisory services [to] help corporations understand and implement best practices in corporate governance, evaluate institutional voting behavior and design executive compensation plans, along with comprehensive risk management solutions for corporate treasurers.”¹² As discussed below, the fact that ISS simultaneously issues advice to both corporations and institutional investors has garnered some criticism.

Recent regulatory and market developments increased the demand for proxy advisory services.¹³ In 2003, the Securities and Exchange Commission (“SEC”) promulgated regulations that require mutual funds to develop voting policies and procedures designed to ensure that the funds’ voting power is exercised in the “best interest” of beneficiaries.¹⁴ In conjunction with these regulations, the SEC adopted rule 30b1-4 under the Investment Company Act of 1940, requiring mutual funds to disclose their complete voting records annually.¹⁵ The rule focused increased attention on mutual fund voting policies.¹⁶ Institutional investor activism also enhanced

10. Daines et al., *supra* note 6, at 2.

11. Joann S. Lublin, *ISS Accepts Bid of \$553 Million from RiskMetrics*, WALL ST. J., Nov. 1, 2006, at A10.

12. RiskMetrics Group, Corporations, <http://www.riskmetrics.com/corporations> (last visited Apr. 20, 2009).

13. See U.S. GOV’T ACCOUNTABILITY OFFICE, REP. NO. GAO-07-765, CORPORATE SHAREHOLDER MEETINGS: ISSUES RELATING TO FIRMS THAT ADVISE INSTITUTIONAL INVESTORS ON PROXY VOTING 6–7 (2007) (describing various regulatory and market developments as leading to growth in the proxy advisory industry). See also PROXY Governance History, <http://www.proxygovernance.com/content/pgi/content/history.shtml> (last visited Apr. 20, 2009) (describing the development of proxy advisory services as “encouraged by a developing regulatory environment that would expand the market for proxy advisory and voting services”).

14. 17 C.F.R. § 275.206(4)-6 (2003).

15. *Id.* § 270.30b1-4.

16. The Department of Labor had previously taken several steps to encourage mutual funds to vote shares in their portfolio companies responsibly. In 1988, the Department advised fund managers that “the decision[s] as to how proxies should be voted . . . are fiduciary acts of plan asset management.” Letter from Alan D. Lebowitz, Deputy Assistant Sec’y, Dep’t of Labor, to Helmuth Fandl, Chairman of the Ret. Bd., Avon Prods., Inc. (Feb. 23, 1988), *in* 15 Pens. Rep. (BNA) 371, 391 (Feb. 29, 1988). The Department reinforced this position in 1990. See Letter from Alan D. Lebowitz, Deputy Assistant Sec’y for Program Operations, Dep’t of Labor, to Robert A. G. Monks, Institutional Shareholder Services, Inc. (Jan. 23, 1990), *in* 17 Pens. Rep. (BNA) 205, 244 (Jan. 29, 1990). It then formalized its policies in an interpretive bulletin in 1994. See Interpretive Bulletins Relating to the Employee Retirement Income Security Act of 1974, 29 C.F.R. § 2509.94-2 (1994), *amended by* 29 C.F.R. § 2509.08-2 (2008). Prior to the SEC’s rule change in 2004, however, these efforts did not

the focus on, and importance of, shareholder voting.

As a result of these developments, several new proxy advisory firms entered the market.¹⁷ GL was founded in 2003.¹⁸ GL provides research and analysis on more than eighteen thousand public companies based in eighty countries around the world.¹⁹ In 2007, GL became a wholly owned subsidiary of the Ontario Teachers' Pension Plan Board.²⁰

EJ was established in 2002 as a division of Egan-Jones Rating Company, an independent company that provides credit ratings information for investors.²¹ EJ "provides research, recommendations and voting services for domestic and foreign proxy proposals offered in annual subscriptions priced according to the number of securities covered."²² EJ provides this coverage for a flat fee of \$12.50 per year per company.²³

PG is a wholly owned subsidiary of FOLIO*fn*, Inc., an innovative financial services company.²⁴ PG began providing recommendations for the 2005 proxy season. Its first subscriber was the Business Roundtable,

receive extensive attention. See CLIFTON D. PETTY, PENSION CONSULTANTS, INC., GATHERING STRENGTH: THE REINFORCEMENT OF FIDUCIARY RESPONSIBILITY FOR PROXY VOTING 1 (2004), available at http://pension-consultants.com/cimages/file_85.pdf (calling the 1994 Interpretive Bulletin "far ahead of its time").

17. The analysis in this Article focuses on the four major proxy advisory firms—ISS, PG, GL, and EJ—which issue publicly reported voting recommendations on a regular basis. Several firms provide related services. For example, CtW Investment Group was organized in February 2006 and provides a limited number of recommendations to union pension funds. CtW's primary efforts are devoted to developing initiatives to support the activism of member pension funds. See CtW Investment Group, Who We Are, <http://www.ctwinvestmentgroup.com/index.php?id=1> (last visited Apr. 20, 2009). Also, Marco Consulting Group, which is included in the GAO Report as one of the major proxy advisory firms, see U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 13, at 8, provides investment consulting services to Taft-Hartley funds and a number of public employee benefit plans. These services include voting its clients' proxies. See Marco Consulting Group, Company History, <http://www.marcoconsulting.com/1.2.html> (last visited Apr. 20, 2009). Marco does not, however, publicly issue voting recommendations. *Id.*

18. About Glass Lewis, <http://www.glasslewis.com/company/index.php> (last visited Apr. 20, 2009).

19. *Id.*

20. *Id.*

21. See About Egan-Jones Proxy, <http://www.ejproxy.com/about.aspx> (last visited Apr. 20, 2009); U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 13, at 8. In 2007, EJ was recognized by the SEC as the fourth "nationally recognized statistical rating organization," a status equivalent to that enjoyed by Moody's, S&P, and Fitch. Order Granting Registration of Egan-Jones Rating Company as a Nationally Recognized Statistical Rating Organization, Exchange Act Release No. 57031, 72 Fed. Reg. 73,909 (Dec. 21, 2007). See also Aaron Lucchetti, *Tiny Firm Gives Ratings Giants Another Worry: Mr. Egan's Ranks Gain Favor as S&P, Fitch, Moody's Draw Scrutiny*, WALL ST. J., Feb. 9, 2008, at B1.

22. About Egan-Jones Proxy, <http://www.ejproxy.com/about.aspx> (last visited Apr. 20, 2009).

23. *Id.*

24. PROXY Governance History, <https://www.proxy.governance.com/content/pgi/content/history.shtml> (last visited Apr. 20, 2009).

which purchased a bulk subscription for its member companies.²⁵

The market for proxy advisory services continues to grow, fueled in part by the increase in institutional ownership of publicly traded equity securities. The overall percentage of institutional holdings rose from 37 percent in 1992 to over 60 percent in 2005.²⁶ Institutional investors are the primary, if not the exclusive, purchasers of proxy advisory services, both because their substantial holdings make the purchase of such services cost efficient and because they may lack the specialized staff or expertise to research voting issues directly.

The SEC's adoption of rule 30b1-4 increased the incentive for mutual funds in particular to purchase advisory services because reliance on the research and recommendations provided by a major proxy advisor is likely to help a mutual fund demonstrate that it has acted with appropriate diligence in exercising its voting power.²⁷ Mutual funds comprise a growing percentage of the institutional investor market—the percentage of U.S. equities owned by mutual funds grew from 7 percent in 1990²⁸ to 32 percent by the end of 2006.²⁹

At the same time, corporate governance changes have increased the significance of shareholder voting. The emergence of hedge fund activism has resulted in a greater number of election contests.³⁰ Even in uncontested elections, shareholder voting has become more important because of the shift from plurality voting to majority voting.³¹ Historically, directors in

25. *Id.*

26. John Authers & Francesco Guerrera, *Institutions Increase Equity Stakes*, FIN. TIMES (London), Jan. 22, 2007, at 27.

27. See 17 C.F.R. § 275.206(4)-6(a) (2003) (requiring that mutual funds “[a]dopt and implement written policies and procedures that are reasonably designed to ensure that [they] vote client securities in the best interest of clients”).

28. BD. OF GOVERNORS OF THE FED. RES. SYS., FLOW OF FUNDS ACCOUNTS OF THE UNITED STATES, FLOWS AND OUTSTANDINGS, SECOND QUARTER 1996, at 88 tbl.L.213 (1996), available at <http://www.federalreserve.gov/releases/z1/19960912/z1.pdf>.

29. BD. OF GOVERNORS OF THE FED. RES. SYS., FLOW OF FUNDS ACCOUNTS OF THE UNITED STATES, FLOWS AND OUTSTANDINGS, FOURTH QUARTER 2006, at 90 tbl.L.213 (2007), available at <http://www.federalreserve.gov/releases/z1/20070308/z1.pdf>. Mutual funds include open-end and closed-end funds as well as exchange-traded funds.

30. Jill E. Fisch, *The Transamerica Case*, in THE ICONIC CASES IN CORPORATE LAW 46, 72 (2008) (stating that “as a result” of increased hedge fund activism, “proxy contests are on the rise”); Alon Brav et al., *Hedge Fund Activism, Corporate Governance, and Firm Performance* 16 (Eur. Corp. Governance Inst., Fin. Working Paper No. 139/2006, 2007), available at <http://ssrn.com/abstract=948907> (recognizing the launching of a proxy election as a hedge fund tactic). For a helpful description of hedge fund activism, see William W. Bratton, *Hedge Funds and Governance Targets*, 95 GEO. L.J. 1375, 1401–09 (2007).

31. See Fisch, *supra* note 30, at 67–70 (describing the adoption and effect of majority voting policies).

most companies were elected by a plurality of the votes cast. Since most elections for directors are uncontested, with the number of nominees equal to the number of vacancies, it took just a single vote to get elected.³² As late as February 2006, 84 percent of S&P 500 companies employed plurality voting.³³ By November 2007, that figure had declined to 34 percent, with 66 percent employing some form of majority voting where nominees must receive more for votes than withhold votes.³⁴ These majority voting requirements for the election of directors create a meaningful opportunity for shareholders to affect the composition of the board by casting a withhold vote without running a full-scale proxy solicitation.³⁵

Other developments that increase the effectiveness of shareholders' votes compound the concerns of directors that are seeking reelection. A proposed New York Stock Exchange ("NYSE") rule change would eliminate the right of brokers to vote stock held in their accounts in uncontested director elections for which they had not received voting instructions.³⁶ Because discretionary broker votes typically are overwhelmingly cast for the board nominees, the proposed change to the NYSE rules would eliminate a large number of automatic for votes for the incumbent management's slate of directors.³⁷ Direct shareholder nomination of directors—a procedure that the SEC has repeatedly

32. See CLAUDIA H. ALLEN, NEAL, GERBER & EISENBERG LLP, STUDY OF MAJORITY VOTING IN DIRECTOR ELECTIONS, at ii (2007), available at <http://www.ngelaw.com/files/upload/majoritystudy111207.pdf>.

33. See *id.* at i.

34. See *id.*

35. Fisch, *supra* note 30, at 71. In her study of majority voting practices, Claudia H. Allen posits that the increased shareholder power that results from majority voting is augmented by developments such as the rise of proxy advisory firms, the fiduciary requirements placed on mutual funds, and the proposed New York Stock Exchange rule discussed below. ALLEN, *supra* note 32, at ii, vi.

36. In 2006, the NYSE submitted a proposed rule change to the SEC that would have eliminated such "discretionary voting" for director elections. See Press Release, N.Y. Stock Exch., NYSE Adopts Proxy Working Group Recommendation to Eliminate Broker Voting in 2008 (Oct. 24, 2006), available at <http://www.nyse.com/press/1161166307645.html>. Although the proposed rule was scheduled to become effective on January 1, 2008, to date, the SEC has not taken action on it. The NYSE recently refiled its proposed rule change, and recent changes in SEC leadership may increase the likelihood that the rule will be approved. Notice of Filing of Proposed Rule Change to Amend NYSE Rule 452 and Listed Company Manual Section 402.08 to Eliminate Broker Discretionary Voting, Exchange Act Release No. 34-59464, 74 Fed. Reg. 9864 (proposed Feb. 26, 2009), available at <http://www.sec.gov/rules/sro/nyse/2009/34-59464.pdf>.

37. See *CiW Investment Group Urges SEC to Promptly Eliminate Broker Votes*, REUTERS, Apr. 17, 2008, <http://www.reuters.com/article/pressRelease/idUS177265+17-Apr-2008+PRN20080417> (explaining that discretionary voting has enabled directors to be reelected solely on the basis of broker votes and has been criticized as "legalized ballot stuffing" by which shareholders are "disenfranchised").

considered but failed to implement³⁸—would substantially increase the ability of shareholders to nominate competing director candidates.

Outside the election of directors, other developments have strengthened the influence of shareholders on company decisions. Shareholder voting on issue proposals, such as bylaw amendments, has become more common. It was only in recent years that shareholder-sponsored governance resolutions began to obtain majority approval. Research finds that issuer implementation of shareholder proposals that receive majority approval has almost doubled since 2002,³⁹ and that outside directors who fail to implement such proposals face an increased likelihood of losing their board seats.⁴⁰ Also, “say on pay” proposals have become one of the most recent and high-profile mechanisms for attempting to address excessive executive compensation.⁴¹

With the growing importance of the shareholder franchise, the influence of proxy advisors has received increased attention. ISS, in particular, has been described as exercising “tremendous clout,”⁴² wielding “extraordinary” influence,⁴³ getting “[w]hatever [it] wants,”⁴⁴ and being able to sway up to 30 percent of the vote in any particular proxy contest.⁴⁵ Because of this influence, issuers and challengers devote substantial effort to meeting with proxy advisors and attempting to win their support.⁴⁶

Coupled with concern about influence is concern about the basis upon which proxy advisors make their recommendations. ISS, in particular, has been criticized for the actual or potential conflicts of interest generated by its corporate consulting. Prominent corporate governance expert Ira Millstein was quoted in the *Wall Street Journal Online* denouncing the

38. See Fisch, *supra* note 30, at 63–67 (describing the SEC’s consideration of proposals to allow shareholder nomination of directors).

39. See Yonca Ertimur, Fabrizio Ferri & Stephen R. Stubben, *Board of Directors’ Responsiveness to Shareholders: Evidence from Shareholder Proposals* 20 (Harvard Bus. Sch., Working Paper No. 08-048, 2008), available at <http://www.hbs.edu/research/pdf/08-048.pdf>.

40. See *id.* at 30–31.

41. See Fisch, *supra* note 30, at 71 (describing “say on pay” initiatives).

42. Dennis K. Berman & Joann S. Lublin, *Advisor ISS Puts Itself on Sale, Could Fetch Up to \$500 Million*, WALL ST. J., Sept. 6, 2006, at C4.

43. Robert D. Hershey, Jr., *A Little Industry with a Lot of Sway on Proxy Votes*, N.Y. TIMES, June 18, 2006, § 3, at 6.

44. William J. Holstein, *Is ISS Too Powerful? And Whose Interests Does It Serve?*, BNET: THE CORNER OFFICE, Feb. 7, 2008, <http://blogs.bnet.com/ceo/?p=1100&tag=content:coll>.

45. *Id.*

46. See, e.g., Tom Johnson, *HP, Compaq Merger Now in Hands of Shareholder Adviser*, REUTERS, Dec. 11, 2001, <http://www.rediff.com/money/2001/dec/11hp.htm> (detailing efforts by both sides to obtain ISS support in the HP-Compaq merger vote and observing that “[m]erging companies typically place a great deal of weight” on meetings with ISS analysts).

conflicts inherent in ISS's business model, stating that "[a]nyone who can't see a conflict between consulting and standards-setting has a problem with their eyesight."⁴⁷ Another commentator described ISS's business model as engendering conflicts of interest similar to those faced by accounting firms that provided auditing and consulting services, observing that "if similar conflicts arose at one of the shareholder meetings it monitors, ISS would or should criticize the issuer."⁴⁸

PG has received criticism similar to that of ISS, primarily because its founding subscriber was the Business Roundtable, an association of corporate CEOs and a prominent pro-issuer advocate.⁴⁹ PG addresses potential conflicts by maintaining a firewall between its proxy advising and corporate clients, but some commentators believe the firm's relationship with issuers "set[s] the stage for potential conflicts of interest."⁵⁰

Some institutional investors have responded to these concerns by choosing proxy advisors that do not provide consulting services. Sensitive to the controversy surrounding ISS's business model, GL and EJ specifically advertise themselves as free of similar conflicts.⁵¹ This policy led the Ohio Public Employees Retirement System ("OPERS") to replace ISS with GL in 2006.⁵²

More subtle issues remain. In particular, although all the major proxy advisors provide general guidelines that purport to explain their voting policies, they describe their processes as employing substantial issuer-specific judgment, and the vast majority of criteria are applied on a case-by-case basis. PG, for example, describes its recommendations as made on

47. Tiffany Kary, *ISS Pressed on Conflict by Governance Expert Millstein*, WALL ST. J., Nov. 16, 2005, http://www.shareholderforum.com/PVN/Library/20051116_WSJ.htm.

48. Robert M. Krasne, *Proxy-Voting Concern: ISS Wields Extraordinary Clout in Recommendations to Investors, Yet Also Provides Services to Corporations*, PENSIONS & INVS., May 31, 2004, at 12, available at <http://www.pionline.com/article/20040531/PRINTSUB/405310706/1026/TOC>.

49. Arden Dale & Kaja Whitehouse, *Legg Mason CEO's Pay Questioned*, WALL ST. J., July 18, 2006, at C11; Bill Baue, *Conflict of Interests Policies and Practices Vary Widely at Proxy Advisory Firms*, SOCIALFUNDS, Apr. 19, 2006, <http://www.socialfunds.com/news/article.cgi/1985.html>.

50. Baue, *supra* note 49.

51. See GLASS, LEWIS & CO., LEADING INDEPENDENT ANALYSIS AND VOTING RECOMMENDATIONS ON GLOBAL PROXIES 2 (2008), available at <http://www.glasslewis.com/downloads/overviews/proxypaper.pdf> ("Glass Lewis does not provide consulting services to corporations, CEOs or directors; as such, Glass Lewis' research is without bias."); Egan-Jones Proxy Services, <http://www.ejproxy.com> (last visited Apr. 20, 2009) ("[T]he integrity of our recommendations is not clouded with the complication of also selling corporate directors and managers consulting services pertaining to these same shareholder proposals.")

52. See Kary, *supra* note 47 (quoting OPERS governance officer Cynthia Richson as stating that ISS had been dismissed "as a result of the 'actual or perceived conflicts'").

an “issue-by-company” basis,⁵³ and it describes eleven factors that it considers “[i]n evaluating whether, in the context of a particular company, [to] recommend a ‘withhold’ vote from certain directors or the entire board.”⁵⁴ Even with respect to practices about which the advisors provide substantial detail, there is no way to determine a specific recommendation from the general policies described. For example, in its 2006 policy updates concerning withhold recommendations for compensation committee members, ISS described itself as shifting from a case-by-case analysis to a “formal policy.”⁵⁵ The formal policy merely consisted, however, of recommending withhold votes if the company had “poor compensation practices”—a standard determined by considering seven case-specific factors.⁵⁶

Thus, although some advisors identify bright-line criteria that determine whether they will issue a withhold recommendation for a director candidate, the majority of the policy guidance they publish consists of a variety of performance and governance factors that will be evaluated or weighed in an undisclosed manner and applied on a company-specific basis.⁵⁷ It is impossible to tell from these lists the relative importance of each factor. Because the lists contain most of the criteria that scholars and governance experts have identified as important, they ultimately provide limited guidance on the advisors’ processes. It is the purpose of this Article to use empirical tests to identify the criteria that appear truly to drive the

53. PROXY Governance, Inc., Policy and Analysis Methodology 1 (unpublished manuscript, available at <http://www.integrityfunds.com/PortalIntegrityFunds/DesktopModules/ViewDocument.aspx?DocumentID=170>) (refusing to take a “one-size-fits-all approach” that does not consider proxy issues in context); PROXY Governance Recommendations on an Issue-by-Company Basis, https://www.proxygovernance.com/content/pgi/content/issue_by_issue.shtml (last visited Apr. 20, 2009) (same).

54. PROXY Governance, Inc., *supra* note 53, at 3–5. PROXY Governance does not explain how these factors will be weighted or combined. *See id.*

55. INSTITUTIONAL S’HOLDER SERVS., ISS U.S. CORPORATE GOVERNANCE POLICY 2006 UPDATES 16 (2005), available at http://media.gibsondunn.com/fstore/documents/pubs/2006_US_Policy_Update_1117051.pdf.

56. *Id.* ISS stated that poor compensation practices “include, but are not limited to, the following:” (1) “[e]gregious employment contracts including excessive severance provisions”; (2) “[e]xcessive perks that dominate compensation”; (3) “[h]uge bonus payouts without justifiable performance linkage”; (4) “[p]erformance metrics that are changed during the performance period”; (5) “[e]gregious SERP (Supplemental Executive Retirement Plans) payouts”; (6) “[n]ew CEO with overly generous new hire package”; (7) “[i]nternal pay disparity”; and (8) “[o]ther excessive compensation payouts or poor pay practices at the company.” *Id.*

57. Even where the criteria appear to be objective, the proxy advisors emphasize that they are examined and applied on a case-by-case basis. *See, e.g.*, Egan-Jones Proxy Services, Proxy Voting Principles and Guidelines 3–5 (unpublished manuscript, on file with authors) (describing policies used in formulating recommendations for directors in uncontested elections).

advisors' recommendations, a task to which this Article now turns.

III. ANALYSIS OF PROXY ADVISORY RECOMMENDATIONS

A. UNIVARIATE ANALYSIS

We analyze empirically the recommendations of the four major proxy advisors—ISS, PG, GL, and EJ—in uncontested director elections. In these elections, there are no competing director candidates, so the advisor either recommends a vote for the director candidate or issues a withhold recommendation. During the time period of this study, most issuers utilized plurality voting, so a withhold recommendation, even if followed, would not directly result in the removal of a director. Nonetheless, a large number of withhold votes, even if technically symbolic, can have a powerful effect. For example, the highly publicized withhold campaign in the 2004 Walt Disney director election resulted in 45 percent of the votes being withheld from Disney's CEO Michael Eisner.⁵⁸ Although Eisner was elected to the board, the company announced six months later that he would retire in 2006.⁵⁹

We focus on uncontested director elections for two reasons. First, the election of directors, who have the power to manage the corporation, is one of the most important governance rights of shareholders and is more significant than a vote on a precatory shareholder resolution.⁶⁰ The board of directors has the power to manage the corporation, and a substantial number of regulatory and policy reforms in recent years have focused on increasing the independence, efficiency, and monitoring capacity of the corporate board.⁶¹ Moreover, several recent studies have shown that boards

58. Jay Sherman, *Eisner Still in Charge, Disney Shareholders Re-Elect Board, Book Stirs Iger Doubts*, TELEVISION WK., Feb. 14, 2005, at 3.

59. *See id.* (reporting Disney's September 2004 announcement that Eisner intended to retire when his contract expired in September 2006).

60. Concededly, shareholder votes on mergers, spin-offs, and similar transactions are very important. By the same token, shareholder votes in contested elections are important, because election contests typically occur in situations involving a control or structural change. *See generally* Cindy R. Alexander et al., *The Role of Advisory Services in Proxy Voting* (Jan. 2008) (unpublished manuscript, available at http://www.law.yale.edu/images/CBL_Workshop/ACSS_proxy_advice_1_2008b_.pdf) (studying the role of proxy advisors in election contests). In transaction-driven votes, however, the shareholder vote is driven largely, if not exclusively, by the perceived economics of the proposed transaction—economics that are company specific. It is impossible to compare a recommendation for a merger at one company with one involving a different transaction at another company.

61. *See* Jeffrey N. Gordon, *The Rise of Independent Directors in the United States, 1950–2005: Of Shareholder Value and Stock Market Prices*, 59 STAN. L. REV. 1465, 1477–1500 (2007) (describing the developments that led to increased board independence beginning in the 1970s).

respond to high withhold votes in director elections by taking actions that are beneficial to shareholders.⁶² Second, unlike other important voting decisions (such as a vote on a merger), director elections are common, which makes it easier to determine the factors that account for a recommendation.

Our dataset examines director elections in 2005 and 2006. We focus only on director elections for U.S. companies listed in the S&P 1500 as of June 30 for the year prior to the relevant director election (June 30, 2004, and June 30, 2005, respectively).

We first examined the factors that affect voting recommendations in a univariate analysis. Using a variety of sources, including academic articles, popular press, policy-governance initiatives, and regulatory proposals and reforms, we attempted to identify the director- and company-specific factors that investors are likely to consider important in formulating their votes. Based on this analysis, for each director in our sample of S&P 1500 companies who received either a for or a withhold recommendation from at least one of the four proxy advisors, we collected the following data about the director's characteristics:⁶³ (1) whether the director was the CEO ("*CEO*"), an employee of the company other than the CEO ("*Empl_Dir*"), an outside director with certain links to the company ("*OutDirLink*"), or a new director ("*New Director*"); (2) whether the director was a member of the audit committee ("*AuditMbr*"), the compensation committee ("*CompMbr*"), or the nominating committee ("*NomMbr*"); and (3) the number of other major company boards on which the director sat ("*ManyBds*"), whether the director attended less than 75 percent of the director meetings ("*Attendance*"), whether the director held at least 20 percent of the company's stock ("*BlockDir*"), whether the director was an interlocking director ("*Interlock*"), whether the director was a nonexecutive chairman of the board ("*Chairman Only*"), and whether the director was seventy-five years old or older ("*Age75*").

62. See, e.g., Paul E. Fischer et al., Investor Perceptions of Board Performance and Board Response to Those Perceptions: Evidence from Uncontested Director Elections 18–28 (Oct. 2008) (unpublished manuscript, available at <http://ssrn.com/abstract=928843>) (finding that boards who perform poorly in elections are more likely to dismiss CEOs, rein in compensation, and scrutinize acquisitions and divestitures). See generally Jie Cai, Jacqueline L. Garner & Ralph A. Walkling, *Electing Directors*, 64 J. FIN. (forthcoming Oct. 2009), available at <http://ssrn.com/abstract=1101924> (finding evidence that boards with low shareholder approval tend to reduce management compensation, dismiss CEOs, and remove takeover defenses); Diane Del Guercio, Laura Seery & Tracie Woidtke, Do Boards Pay Attention When Institutional Investor Activists “Just Vote No”? (Jan. 2008) (unpublished manuscript, available at <http://ssrn.com/abstract=575242>) (finding a correlation between “vote no” campaigns and subsequent improvements in operating performance).

63. See *infra* app.

TABLE 1. Sample Summary

Advisory Firm	N	Number of W/H Recs.	Number of For Recs.	W/H Rate	t-statistic W/H Rate = ISS W/H Rate	t-statistic W/H Rate = PG W/H Rate	t-statistic W/H Rate = GL W/H Rate
All	16,038						
ISS	13,869	917	12,953	0.066			
PG	5,437	202	5,235	0.037	-8.7***		
GL	15,722	2,956	12,766	0.188	32.4***	37.4***	
EJ	14,147	1,551	12,596	0.110	12.9***	19.7***	-19.2***

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

In addition, for each company and each year, we collected data from SEC filings, press releases, the Investor Responsibility Research Center (“IRRC”) Governance Database, the Georgeson Annual Corporate Governance Reviews, and the Center for Research in Security Prices (“CRSP”) on the following company-specific factors: (1) whether the first public report of a restatement to a company’s financial statement occurred within two years prior to the annual meeting (“*Prior Restat*”), whether the first public statement of an SEC investigation or enforcement action occurred within two years prior to the annual meeting (“*Prior SEC*”), and whether the company rejected an issue proposal that had received majority shareholder support in the previous year (“*IP No*”); (2) whether the company had a classified board (“*ClassBd*”), a poison pill (“*PPill*”), cumulative voting (“*CumVote*”), or golden parachutes (“*GP*”); (3) whether the company was in the top or bottom 5 percent of companies ranked based on abnormal holding period returns for the three-year period prior to the meeting date for the year of the recommendation, adjusted based on the CRSP value-weighted market index (“*Top5AbRet*,” “*Bot5AbRet*”); and (4) whether the CEO of the company was in the top 5 percent of total excess compensation (“*Top5AbComp*”).

Table 1 provides some summary statistics about the coverage and withhold ratios for each of the four proxy advisors. We found that the advisors differed substantially in the percentage of withhold recommendations they issued. ISS issued withhold recommendations for 6.6% of the directors in the sample, PG for 3.7%, GL for 18.8%, and EJ for 11.0%. The difference in withhold percentages for each pair of advisors is statistically significant at the 1% level.

To see how specific director and company attributes related to the likelihood of a withhold, we tabulated in tables 2.1–2.4 the voting recommendations for directors along several dimensions, and calculated for each proxy advisor whether the likelihood that a director with a certain

attribute (for example, a CEO) received a withhold recommendation from a certain advisor (for example, ISS) was significantly higher or lower than the average for that advisor.

We divided the attributes into several categories and subcategories: (1) audit/disclosure-related attributes (audit committee member, prior restatement, prior SEC investigation); (2) compensation-related attributes (compensation committee member, top 5% abnormal compensation); (3) board-related attributes with the following subcategories: board effectiveness (attendance, many boards, age greater than 75), board composition (nominating committee member), board independence (employee director, outside linked director, block director, interlocking director, chairman only), and board responsiveness (shareholder proposal ignored); (4) takeover-related attributes (classified board, poison pill, cumulative voting, and golden parachutes); (5) performance-related attributes (bottom 5% abnormal return, top 5% abnormal return); and (6) uncategorized attributes (whether the director was a new director or the CEO).

Since each advisor issues many more for than withhold recommendations, we posit that withhold recommendations are triggered by specific problems, either problems with a specific director or issuer-level concerns. Several attributes in tables 2.1–2.4 reflect problems (or an increased likelihood of a problem) that we expect would be important to investors in deciding how to vote and should therefore affect the voting recommendations issued by proxy advisors. For example, commentators have identified low attendance and multiple board positions as factors correlated with reduced director effectiveness.⁶⁴ Older directors may be less energetic or involved.⁶⁵ Director performance may be impaired by a lack of independence or the presence of conflicts of interest (such directors may include employee directors other than the CEO,⁶⁶ outside directors with linked affiliations with the company, directors with substantial block

64. See, e.g., John K. Wells, *Multiple Directorships: The Fiduciary Duties and Conflicts of Interest That Arise When One Individual Serves More Than One Corporation*, 33 J. MARSHALL L. REV. 561, 581 (2000) (“More and more corporate watchdogs call for directors to limit the number of boards on which they serve.”); *CPP Investment Board Releases Proxy Voting Guidelines*, CANADIAN CORP. NEWSWIRE, Feb. 24, 2003 (identifying poor meeting attendance as an indicator of potential director ineffectiveness).

65. See, e.g., *Useless at 70? Trends in Mandatory Director Retirement*, ALLBUSINESS, Oct. 1, 2001, <http://www.allbusiness.com/business-planning-structures/business-structures/958172-1.html> (reporting age limits and mandatory retirement policies among publicly traded companies).

66. Since it is generally accepted that CEOs should be on the board of their companies, their presence does not raise similar issues.

shareholdings, and directors that have interlocking board relationships with the company).

Potential company-specific problems include poor governance and poor performance. Poor performance may be an important factor contributing to shareholder dissatisfaction with the existing directors. Shareholders may become dissatisfied with unresponsive directors, as evidenced by a failure to adopt a shareholder proposal that has received majority support.⁶⁷ Shareholders may also view directors as unresponsive or entrenched if the company has a high level of antitakeover protection.⁶⁸

With respect to company problems, some directors may be viewed by shareholders as more responsible than others. Directors who sit on certain key committees may be held responsible for problems associated with that committee's function.⁶⁹ In particular, members of audit committees may be held more responsible for audit-related problems such as restatements and thus be more likely to receive a withhold recommendation. Compensation committee members may be held more accountable for excessive executive pay. New directors may be viewed as less responsible for company-level problems because such problems did not arise on their watch.

It is difficult to predict how shareholders will view the responsibility of the CEO for issuer-specific problems, but we posit that CEOs will be viewed as having greater responsibility for corporate performance. On the other hand, given the more severe implications of not reelecting a CEO to the board, investors may view a withhold vote from a CEO as a more economically significant event and be wary of casting such votes.

For each of the four proxy advisory firms, tables 2.1–2.4 report (as “% Total”) the frequency of each attribute as a percentage of each proxy advisor's recommendations. For example, ISS made 1344 recommendations for directors who are also CEOs and 12,917 recommendations in total (where data exist on whether the director is a CEO or not) for a % ISS Total of 10.40%. Tables 2.1–2.4 also report the number of withhold recommendations for directors with the particular

67. See Ertimur et al., *supra* note 39, at 30 (finding outside directors who failed to adopt a shareholder proposal were more likely to be removed).

68. For an examination of the relationship between antitakeover and other entrenchment devices and equity prices, see Paul Gompers, Joy Ishii & Andrew Metrick, *Corporate Governance and Equity Prices*, 118 Q.J. ECON. 107 (2003).

69. Shareholders may, in particular, impose greater accountability on directors with specialized expertise. See Jill E. Fisch & Caroline M. Gentile, *The Qualified Legal Compliance Committee: Using the Attorney Conduct Rules to Restructure the Board of Directors*, 53 DUKE L.J. 517, 561–63 (2003) (assessing the effectiveness of using “expert” directors on specialized board committees).

TABLE 2.1. Summary Statistics on ISS Withhold Recommendations

<i>Attribute</i>	<i>Category</i>	<i>Predicted Effect on W/H Recs.</i>	<i>ISS Tot. Recs.</i>	<i>ISS Att. Recs.</i>	<i>% ISS Total</i>	<i>ISS Tot. W/H</i>	<i>ISS Att. W/H</i>	<i>% ISS W/H</i>	<i>Diff. Between % ISS W/H and % ISS Total</i>
All Directors			13,869	13,869	100.00	916	916	100.00	
<i>CEO</i>	General	?	12,917	1344	10.40	839	74	8.82	-1.58
<i>New Director</i>	General	-	13,869	2023	14.59	916	53	5.79	-8.80***
<i>AuditMbr</i>	Audit	+	12,829	5105	39.79	831	233	28.04	-11.75***
<i>Prior Restat</i>	Audit	+	13,869	1671	12.05	916	102	11.14	-0.91
<i>Prior SEC</i>	Audit	+	13,869	1005	7.25	916	81	8.84	1.60*
<i>CompMbr</i>	Compensation	+	12,829	4919	38.34	831	351	42.24	3.90**
<i>Top5AbComp</i>	Compensation	+	13,267	657	4.95	868	65	7.49	2.54***
<i>Attendance</i>	Board Effect.	+	12,798	81	0.63	831	36	4.33	3.70***
<i>ManyBds</i>	Board Effect.	+	12,473	1221	9.79	797	120	15.06	5.27***
<i>Age75</i>	Board Effect.	+	13,869	1473	10.62	916	132	14.41	3.79***
<i>NomMbr</i>	Board Comp.	+	12,829	5042	39.30	831	349	42.00	2.70
<i>Empl_Dir</i>	Board Indep.	+	12,829	804	6.27	831	86	10.35	4.08***
<i>OutDirLink</i>	Board Indep.	+	12,829	1358	10.59	831	268	32.25	21.66***
<i>BlockDir</i>	Board Indep.	+	12,812	107	0.84	831	28	3.37	2.53***
<i>Interlock</i>	Board Indep.	+	12,829	33	0.26	831	3	0.36	0.10
<i>Chairman Only</i>	Board Indep.	-	12,917	286	2.21	839	19	2.26	0.05
<i>IP No</i>	Board Resp.	+	13,869	135	0.97	916	67	7.31	6.34***
<i>ClassBd</i>	Takeover	+	13,647	5074	37.18	908	364	40.09	2.91*
<i>PPill</i>	Takeover	+	13,647	7014	51.40	908	436	48.02	-3.38**
<i>CumVote</i>	Takeover	+	13,647	1526	11.18	908	116	12.78	1.59
<i>GP</i>	Takeover	+	13,647	10,238	75.02	908	569	62.67	-12.35***
<i>Bot5AbRet</i>	Performance	+	13,847	526	3.80	916	47	5.13	1.33**
<i>Top5AbRet</i>	Performance	-	13,847	744	5.37	916	59	6.44	1.07

Note: "% ISS Total" is defined as the ratio of ISS recommendations for the specific attribute ("ISS Att. Recs.") over the total number of ISS recommendations where data exist for the specific attribute ("ISS Tot. Recs."). The definition of "% PG Total," "% GL Total," and "% EJ Total" is analogous. "% ISS W/H" is defined as the ratio of ISS withhold recommendations for the specific attribute ("ISS Att. W/H") over the total number of ISS withhold recommendations where data exist for the specific attribute ("ISS Tot. W/H"). The definition of "% PG W/H," "% GL W/H," and "% EJ W/H" is analogous.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$ (from a χ^2 test of the null hypothesis that there is no difference between the proportion of ISS recommendations (for or W/H) for a specific attribute (for example, CEO) relative to all ISS recommendations (for or W/H) and the proportion of ISS withhold recommendations for a specific attribute relative to all ISS withhold recommendations)

TABLE 2.2. Summary Statistics on PG Withhold Recommendations

<i>Attribute</i>	<i>Category</i>	<i>Predicted Effect on W/H Recs.</i>	<i>PG Tot. Recs.</i>	<i>PG Att. Recs.</i>	<i>% PG Total</i>	<i>PG Tot. W/H</i>	<i>PG Att. W/H</i>	<i>% PG W/H</i>	<i>Diff. Between % PG W/H and % PG Total</i>
All Directors			5437	5437	100.00	202	202	100.00	
<i>CEO</i>	General	?	5078	528	10.40	182	5	2.75	-7.65***
<i>New Director</i>	General	-	5437	816	15.01	202	8	3.96	-11.05***
<i>AuditMbr</i>	Audit	+	5047	2014	39.90	182	74	40.66	0.75
<i>Prior Restat</i>	Audit	+	5437	655	12.05	202	11	5.45	-6.60***
<i>Prior SEC</i>	Audit	+	5437	324	5.96	202	16	7.92	1.96
<i>CompMbr</i>	Compensation	+	5047	1949	38.62	182	150	82.42	43.80***
<i>Top5AbComp</i>	Compensation	+	5236	289	5.52	190	45	23.68	18.16***
<i>Attendance</i>	Board Effect.	+	5040	40	0.79	182	6	3.30	2.50***
<i>ManyBds</i>	Board Effect.	+	5042	470	9.32	180	23	12.78	3.46
<i>Age75</i>	Board Effect.	+	5437	558	10.26	202	35	17.33	7.06***
<i>NomMbr</i>	Board Comp.	+	5047	2003	39.69	182	87	47.80	8.12**
<i>Empl_Dir</i>	Board Indep.	+	5047	305	6.04	182	2	1.10	-4.94***
<i>OutDirLink</i>	Board Indep.	+	5047	525	10.40	182	18	9.89	-0.51
<i>BlockDir</i>	Board Indep.	+	5047	52	1.03	182	4	2.20	1.17
<i>Interlock</i>	Board Indep.	+	5047	10	0.20	182	0	0.00	-0.20
<i>Chairman Only</i>	Board Indep.	-	5078	104	2.05	182	0	0.00	-2.05*
<i>IP No</i>	Board Resp.	+	5437	65	1.20	202	6	2.97	1.77**
<i>ClassBd</i>	Takeover	+	5330	1932	36.25	193	66	34.20	-2.05
<i>PPill</i>	Takeover	+	5330	2929	54.95	193	108	55.96	1.01
<i>CumVote</i>	Takeover	+	5330	634	11.89	193	27	13.99	2.09
<i>GP</i>	Takeover	+	5330	4008	75.20	193	153	79.27	4.08
<i>Bot5AbRet</i>	Performance	+	5432	262	4.82	200	1	0.50	-4.32***
<i>Top5AbRet</i>	Performance	-	5432	306	5.63	200	10	5.00	-0.63

Note: See notes to table 2.1.

TABLE 2.3. Summary Statistics on GL Withhold Recommendations

<i>Attribute</i>	<i>Category</i>	<i>Predicted Effect on W/H Recs.</i>	<i>GL Tot. Recs.</i>	<i>GL Att. Recs.</i>	<i>% GL Total</i>	<i>GL Tot. W/H</i>	<i>GL Att. W/H</i>	<i>%GL W/H</i>	<i>Diff. Between % GL W/H and % GL Total</i>
All Directors			15,722	15,722	100.00	2956	2956	100.00	
<i>CEO</i>	General	?	14,526	1526	10.51	2673	58	2.17	-8.34***
<i>New Director</i>	General	-	15,722	2295	14.60	2956	172	5.82	-8.78***
<i>AuditMbr</i>	Audit	+	14,436	5765	39.93	2662	1223	45.94	6.01***
<i>Prior Restat</i>	Audit	+	15,722	1914	12.17	2956	499	16.88	4.71***
<i>Prior SEC</i>	Audit	+	15,722	1115	7.09	2956	254	8.59	1.50***
<i>CompMbr</i>	Compensation	+	14,436	5558	38.50	2662	1249	46.92	8.42***
<i>Top5AbComp</i>	Compensation	+	15,005	745	4.97	2782	169	6.00	1.04**
<i>Attendance</i>	Board Effect.	+	14,396	98	0.68	2660	73	2.74	2.06***
<i>ManyBds</i>	Board Effect.	+	13,742	1302	9.47	2527	344	13.61	4.14***
<i>Age75</i>	Board Effect.	+	15,722	1770	11.26	2956	424	14.34	3.09***
<i>NomMbr</i>	Board Comp.	+	14,436	5665	39.24	2662	1299	48.80	9.56***
<i>Empl_Dir</i>	Board Indep.	+	14,436	930	6.44	2662	180	6.76	0.32
<i>OutDirLink</i>	Board Indep.	+	14,436	1523	10.55	2662	587	22.05	11.50***
<i>BlockDir</i>	Board Indep.	+	14,419	123	0.85	2656	29	1.09	0.24
<i>Interlock</i>	Board Indep.	+	14,436	36	0.25	2662	27	1.01	0.76***
<i>Chairman Only</i>	Board Indep.	-	14,526	329	2.26	2673	36	1.35	-0.92***
<i>IP No</i>	Board Resp.	+	15,722	146	0.93	2956	44	1.49	0.56***
<i>ClassBd</i>	Takeover	+	15,423	5577	36.16	2873	998	34.74	-1.42
<i>PPill</i>	Takeover	+	15,423	7902	51.24	2873	1426	49.63	-1.60
<i>CumVote</i>	Takeover	+	15,423	1683	10.91	2873	291	10.13	-0.78
<i>GP</i>	Takeover	+	15,423	11,530	74.76	2873	2072	72.12	-2.64***
<i>Bot5AbRet</i>	Performance	+	15,717	794	5.05	2956	230	7.78	2.73***
<i>Top5AbRet</i>	Performance	-	15,717	794	5.05	2956	141	4.77	-0.28

Note: See notes to table 2.1.

TABLE 2.4. Summary Statistics on EJ Withhold Recommendations

<i>Attribute</i>	<i>Category</i>	<i>Predicted Effect on W/H Recs.</i>	<i>EJ Tot. Recs.</i>	<i>EJ Att. Recs.</i>	<i>% EJ Total</i>	<i>EJ Tot. W/H</i>	<i>EJ Att. W/H</i>	<i>% EJ W/H</i>	<i>Diff. Between % EJ W/H and % EJ Total</i>
All Directors			14,147	14,147	100.00	1551	1551	100.00	
<i>CEO</i>	General	?	12,981	1340	10.32	1419	43	3.03	-7.29***
<i>New Director</i>	General	-	14,147	2032	14.36	1551	135	8.70	-5.66***
<i>AuditMbr</i>	Audit	+	12,892	5108	39.62	1405	551	39.22	--0.40
<i>Prior Restat</i>	Audit	+	14,147	1614	11.41	1551	157	10.12	-1.29
<i>Prior SEC</i>	Audit	+	14,147	1070	7.56	1551	139	8.96	1.40*
<i>CompMbr</i>	Compensation	+	12,892	4909	38.08	1405	642	45.69	7.62***
<i>Top5AbComp</i>	Compensation	+	13,597	745	5.48	1502	116	7.72	2.24***
<i>Attendance</i>	Board Effect.	+	12,854	84	0.65	1403	47	3.35	2.70***
<i>ManyBds</i>	Board Effect.	+	12,439	1235	9.93	1362	537	39.43	29.50***
<i>Age75</i>	Board Effect.	+	14,147	1683	11.90	1551	201	12.96	1.06
<i>NomMbr</i>	Board Comp.	+	12,892	5047	39.15	1405	698	49.68	10.53***
<i>Empl_Dir</i>	Board Indep.	+	12,892	826	6.41	1405	47	3.35	-3.06***
<i>OutDirLink</i>	Board Indep.	+	12,892	1359	10.54	1405	377	26.83	16.29***
<i>BlockDir</i>	Board Indep.	+	12,875	98	0.76	1404	27	1.92	1.16***
<i>Interlock</i>	Board Indep.	+	12,892	33	0.26	1405	4	0.28	0.03
<i>Chairman Only</i>	Board Indep.	-	12,981	292	2.25	1419	30	2.11	-0.14
<i>IP No</i>	Board Resp.	+	14,147	133	0.94	1551	15	0.97	0.03
<i>ClassBd</i>	Takeover	+	13,916	4987	35.84	1526	493	32.31	-3.53***
<i>PPill</i>	Takeover	+	13,916	7098	51.01	1526	715	46.85	-4.15***
<i>CumVote</i>	Takeover	+	13,916	1514	10.88	1526	147	9.63	-1.25
<i>GP</i>	Takeover	+	13,916	10,455	75.13	1526	1119	73.33	-1.80
<i>Bot5AbRet</i>	Performance	+	14,147	566	4.00	1551	57	3.68	-0.33
<i>Top5AbRet</i>	Performance	-	14,147	741	5.24	1551	62	4.00	-1.24**

Note: See notes to table 2.1.

attribute (“Att. W/H”) and the extent to which that attribute is reflected in the total number of withhold recommendations (“% W/H”) (where data exist for the attribute in question). For example, ISS issued 74 withhold recommendations for CEO directors, which accounted for 8.82% of the total number of ISS withhold recommendations where data exist on whether the director is a CEO.

Tables 2.1–2.4 then provide the difference between % W/H and % Total. This difference gives a measure of the relative effect of this attribute on the likelihood of a withhold recommendation. With respect to ISS, for example, the difference is equal to -1.58 percentage points for CEOs. This difference is not significant, indicating that CEOs are not less likely to receive an ISS withhold recommendation than average directors. We provide similar statistics for PG, GL, and EJ recommendations.

As tables 2.1–2.4 show, both director and company attributes are associated with recommendations, largely in the predicted direction. The results suggest, however, that different proxy advisors are concerned with different categories. ISS seems to be most concerned about board-related factors generally. Of the ten board-related factors, seven are associated with a significantly increased probability of a withhold recommendation (all at the 1% level). Secondly, ISS appears concerned about performance- and compensation-related factors (*CompMbr* and *Bot5AbRet* are both significant at the 5% level, and *Top5AbComp* is significant at the 1% level). By contrast, neither takeover- nor audit/disclosure-related factors are consistently significant in the predicted direction.

PG, although generally least likely to issue withhold recommendations, seems to be particularly concerned with compensation. Both compensation-related factors (*CompMbr* and *Top5AbComp*) are significant at the 1% level and numerically important. Several board-related factors—*Age75*, *Attendance*, and *IP No*—are also significant. Employee directors (as well as CEOs) are less likely than average to receive a withhold recommendation (possibly due to the fact that they do not sit on compensation committees). Audit/disclosure-, performance-, and takeover-related factors are not associated with an increased likelihood of a PG withhold recommendation.

GL issues the largest number of withhold recommendations. GL seems to pay particular attention to audit/disclosure-related factors (each of the three factors is significant at the 1% level) and performance-related factors (*Bot5AbRet* is significant in the predicted direction at the 1% level). In addition, most board-related factors (eight of ten) and both

compensation-related factors are significant. Takeover-related factors are not associated with an increased likelihood of a withhold recommendation.

EJ appears to place weight on factors related to compensation (both factors are significant at the 1% level), board effectiveness (two of three are significant at the 1% level), and board composition (*NomMbr* is significant at the 1% level). Although being an outside linked director (*OutDirLink*) is associated with a statistically and economically significant increase in the likelihood of a withhold recommendation, being an employee director (*Empl_Dir*) is associated with a significant *decrease* in the likelihood of a withhold recommendation. EJ also seems relatively unconcerned about audit/disclosure-, performance-, and takeover-related factors.

B. BASE REGRESSIONS

We next estimate a logit model for each of the proxy advisors with the recommendation by the advisor as a dependent variable (withhold = 1 and for vote = 0) and the director and company attributes in tables 2.1–2.4 as independent variables. In addition, we control for three factors: the year in which the recommendation was made (*Year06*), the standard deviation in the company's stock return measured for the one-year period prior to the annual meeting date for the year in which the recommendation was made (*Sdret*), and the log of the market capitalization of the firm (*ln(market capitalization)*). The results of the logit models are reported in table 3. In table 3, we also report in brackets the marginal effect on the probability of a withhold recommendation for each factor, calculated in each case at the mean of the other factors. For example, for ISS, being a CEO increases the probability of a withhold recommendation by 3.5% if each of the other factors is at its mean level. Unless otherwise noted, all reported statistics are based on two-sided tests.

Overall, the regression results are stronger than those of the univariate analysis. Of eighty-five variables for which we developed a one-sided hypothesis and obtained estimates, forty-six are significant in the predicted direction, but only two are significant in the opposite direction (compared with ten in tables 2.1–2.4).

TABLE 3. Base Model

<i>Attribute</i>	<i>Category</i>	<i>VoteISS</i>	<i>VotePG</i>	<i>VoteGL</i>	<i>VoteEI</i>
<i>CEO</i>	General	0.689*** (3.86) [0.035]	-0.101 (-0.25) [-0.002]	-1.087*** (-6.11) [-0.101]	-0.307 (-1.48) [-0.019]
<i>New Director</i>	General	-0.746*** (-4.18) [-0.024]	-1.150*** (-3.44) [-0.013]	-1.065*** (-10.99) [-0.104]	-0.170 (-1.42) [-0.011]
<i>AuditMbr</i>	Audit	-0.0599 (-0.55) [-0.002]	0.179 (0.96) [0.003]	0.446*** (6.81) [0.058]	0.196** (2.27) [0.013]
<i>Prior Restat</i>	Audit	-0.292 (-1.31) [-0.010]	-0.759 (-1.23) [-0.009]	0.406*** (3.99) [0.057]	-0.397*** (-2.72) [-0.023]
<i>Prior SEC</i>	Audit	0.230 (0.79) [0.010]	0.787 (1.42) [0.018]	0.329** (2.22) [0.046]	0.235 (1.41) [0.017]
<i>CompMbr</i>	Compensation	0.533*** (4.59) [0.022]	2.169*** (5.13) [0.051]	0.384*** (5.82) [0.050]	0.413*** (4.76) [0.029]
<i>Top5AbComp</i>	Compensation	0.614* (1.78) [0.031]	2.220*** (5.22) [0.102]	0.320** (2.03) [0.044]	0.368** (2.28) [0.028]
<i>Attendance</i>	Board Effect.	2.903*** (10.01) [0.394]	1.690*** (2.99) [0.064]	2.679*** (10.45) [0.567]	2.975*** (11.04) [0.529]
<i>ManyBds</i>	Board Effect.	0.826*** (5.96) [0.045]	0.512* (1.75) [0.010]	0.530*** (6.54) [0.077]	2.424*** (24.82) [0.350]
<i>Age75</i>	Board Effect.	0.136 (0.68) [0.006]	0.966*** (2.66) [0.024]	0.243* (1.95) [0.033]	-0.00849 (-0.05) [-0.001]
<i>NomMbr</i>	Board Comp.	0.356*** (3.33) [0.015]	-0.210 (-1.13) [-0.003]	0.344*** (5.93) [0.044]	0.534*** (6.84) [0.038]
<i>Empl_Dir</i>	Board Indep.	1.585*** (6.52) [0.122]	0.146 (0.15) [0.003]	1.036*** (7.92) [0.174]	0.417 (1.50) [0.033]
<i>OutDirLink</i>	Board Indep.	1.976*** (12.08) [0.167]	0.245 (0.47) [0.004]	1.422*** (15.73) [0.252]	1.884*** (15.51) [0.236]
<i>BlockDir</i>	Board Indep.	1.039*** (2.97) [0.067]	2.165** (2.00) [0.107]	0.593** (1.97) [0.090]	1.532*** (3.68) [0.191]

TABLE 3 (continued)

<i>Attribute</i>	<i>Category</i>	<i>VoteISS</i>	<i>VotePG</i>	<i>VoteGL</i>	<i>VoteEI</i>
<i>Interlock</i>	Board Indep.	-0.754 (-1.23) [-0.021]	...	1.787*** (3.78) [-0.360]	-1.076 (-1.25) [-0.047]
<i>Chairman Only</i>	Board Indep.	-0.767** (-2.48) [-0.022]	...	-1.112*** (-4.65) [-0.095]	0.0708 (0.26) [0.005]
<i>IP No</i>	Board Resp.	3.028*** (6.17) [0.422]	1.432 (1.57) [0.047]	0.851*** (3.01) [0.140]	-0.553 (-1.20) [-0.030]
<i>ClassBd</i>	Takeover	0.334** (2.18) [0.014]	0.0335 (0.10) [0.001]	-0.0169 (-0.25) [-0.002]	-0.0347 (-0.38) [-0.002]
<i>PPill</i>	Takeover	-0.0145 (-0.09) [-0.001]	-0.0683 (-0.19) [-0.001]	-0.0132 (-0.19) [-0.002]	-0.0494 (-0.53) [-0.003]
<i>CumVote</i>	Takeover	0.381* (1.83) [0.017]	0.269 (0.66) [0.005]	-0.108 (-0.90) [-0.013]	-0.0140 (-0.11) [-0.001]
<i>GP</i>	Takeover	-0.557*** (-3.24) [-0.025]	0.398 (1.04) [0.006]	-0.115 (-1.42) [-0.015]	-0.0585 (-0.56) [-0.004]
<i>Top5AbRet</i>	Performance	-0.0534 (-0.18) [-0.002]	-1.359* (-1.92) [-0.013]	-0.280 (-1.52) [-0.032]	-0.193 (-1.11) [-0.012]
<i>Bot5AbRet</i>	Performance	0.369 (1.27) [0.017]	...	0.393*** (2.87) [0.056]	0.133 (0.60) [0.009]
<i>Sdret</i>		28.56*** (2.90) [1.124]	20.83 (1.01) [0.328]	12.97*** (2.64) [1.626]	-1.915 (-0.26) [-0.128]
<i>ln(market cap.)</i>		-0.0839 (-1.40) [-0.003]	-0.0236 (-0.21) [-0.000]	-0.0662** (-2.31) [-0.008]	0.0803** (2.12) [0.005]
<i>Year06</i>		-0.126 (-0.95) [-0.005]	0.162 (0.72) [0.003]	0.145** (2.34) [0.018]	-0.224*** (-3.07) [-0.015]
Constant		-3.454*** (-5.31)	-5.561*** (-3.74)	-1.996*** (-6.27)	-3.856*** (-8.17)
<i>N</i>		11,833	4509	12,973	11,809
pseudo <i>R</i> ²		0.152	0.198	0.106	0.206

Note: *t*-statistics are in parentheses; marginal probabilities (calculated with all other variables set at their mean) are in brackets. Marginal probabilities are calculated using Stata's *mfx* command. Where data are not available, ellipsis dots are inserted.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

1. ISS

The results for ISS are largely consistent with those from the univariate analysis. Of the ten board-related factors, eight are significant in the predicted direction. Furthermore, as reported in table 3, several of the board-related factors have a material economic impact on the likelihood of a withhold recommendation. This is true for factors that affect relatively few directors,⁷⁰ such as *IP No* (42.2 percentage point increase) or *Attendance* (39.4 percentage point increase); but notably it is also true for factors that affect an intermediate number of directors, such as *Empl_Dir* (6.3% of the sample of ISS recommendations, 12.2 percentage point increase in probability) or *OutDirLink* (10.6% of the ISS sample, 16.7 percentage point increase).

Among the compensation-related factors, membership on the compensation committee (*CompMbr*) is statistically significant, but has a small quantitative impact. Contrary to the univariate results and to the logit models for the other proxy advisors, CEOs are *more* likely to receive withhold recommendations from ISS. None of the audit/disclosure- or performance-related factors is significant. Of the takeover-related factors, golden parachutes (*GP*) are associated with a significant decrease in the likelihood of a withhold recommendation (at the 1% level), and classified boards (*ClassBd*) and cumulative voting (*CumVote*) are associated with a significant increase (at the 5% and 10% levels, respectively). New directors are less likely to receive withhold recommendations.

2. PG

For PG, the regressions confirm the importance it places on compensation. Membership on the compensation committee (*CompMbr*) and top 5% abnormal compensation (*Top5AbComp*) are highly significant and yield high coefficient estimates. The marginal effects of *CompMbr* and *Top5AbComp* on the probability of a withhold recommendation are substantially higher than those for ISS—respectively, 5.1% versus 2.2% for compensation committee members (38.6% of the PG sample) and 10.2% versus 3.1% for top 5% abnormal compensation (5.5% of the PG sample). Of the eight board-related variables for which we could obtain estimates,⁷¹

70. We define a factor as affecting relatively few directors if it affects less than 1% of the sample.

71. Both *Interlock* = 1 and *Chairman Only* = 1 were perfectly correlated with a for recommendation by PG and, as a result, were dropped from the sample.

all three board effectiveness variables are significant at varying levels, and the variable for block director is significant at the 5% level. But the board-related variables either affect only few directors (*Attendance* and *BlockDir*) or have only a small marginal effect on the probability of a withhold recommendation (*ManyBds* and *Age75*). Top 5% abnormal return (*Top5AbRet*) is associated with a marginal (both statistically and economically) reduction in the likelihood of a withhold recommendation; bottom 5% abnormal return (*Bot5AbRet*) was dropped from the regressions because it was perfectly correlated with a for recommendation. Neither CEO status nor any of the audit/disclosure- or takeover-related factors is significant. New directors are less likely to receive a withhold recommendation.

3. GL

For GL, all audit/disclosure-related factors are significant, as are all ten board-related factors (all in the predicted direction). Membership on the compensation committee (*CompMbr*) and top 5% abnormal CEO compensation (*Top5AbComp*) are also significant, as is the indicator variable for bottom 5% abnormal returns (*Bot5Ret*). None of the takeover-related factors is significant. In terms of marginal effect, board-, audit/disclosure-, performance-, and compensation-related factors are all highly significant. New directors are less likely to receive a withhold recommendation.

4. EJ

The regression results for EJ confirm its focus on compensation (*CompMbr* and *Top5AbComp* are significant). As for board-related attributes, the regression results indicate a focus on composition (*NomMbr* is significant) as well as effectiveness (two of three attributes are significant, as in the univariate test). EJ also appears to focus on board independence (*OutDirLink* and *BlockDir* are significantly positive), but not board responsiveness (*IP No* is insignificant). In terms of marginal effect, the most important factors—considering both their impact and the number of directors affected—are *OutDirLink* (10.5% of the sample of EJ recommendations, 23.6% increase in the likelihood of a withhold recommendation), *ManyBds* (9.9% of the EJ sample, 35.0% increase in likelihood), and *NomMbr* (39.2% of the EJ sample, 3.8% increase in likelihood). Of the audit/disclosure-related factors, being a member of the audit committee increases the likelihood of a withhold recommendation, but having had a restatement *decreases* that likelihood. None of the

TABLE 4. Summary of Results

<i>Weight</i>	<i>ISS</i>	<i>PG</i>	<i>GL</i>	<i>EJ</i>
Focus	Board	Compensation	Audit	Eclectic
Primary Factors	Board (generally)	Compensation	Audit Board (generally) Compensation Performance	Board (selective)
Secondary Factors	Compensation	Board (effect.) Block Director		Compensation
No Effect or Inconsistent Treatment	Audit Performance Takeover	Audit Board (other) Takeover Performance	Takeover	Audit Board (resp.) Takeover

performance- or takeover-related factors is significant, nor is being a CEO or new director.

C. SUMMARY OF DIFFERENCES BETWEEN PROXY ADVISORS

Table 4 summarizes and compares the factors that affect recommendations by the four proxy advisors. Overall, other than takeovers, each category is important for at least one proxy advisor, and two categories—compensation and board effectiveness—are at least secondary factors for each of the proxy advisors. Nevertheless, there are important differences among the advisors. ISS stands out in its attention to board-related factors, paying less relative attention to compensation-related factors than PG and GL, and apparently no attention to audit/disclosure-related factors. PG's primary focus, by contrast, is on compensation, to which it attributes greater weight than it does to other factors and than do other proxy advisors. GL distinguishes itself from the other proxy advisors by the significant weight it places on audit/disclosure-related factors, which the other proxy advisors either ignore or (in the case of EJ) treat inconsistently. EJ is the most eclectic of the proxy advisors. It gives weight to selective board-related factors (but less consistently so than do ISS and GL), as well as to compensation-related factors (but less so than PG), and treats audit/disclosure-related factors inconsistently.

IV. REGRESSIONS WITH INTERACTION VARIABLES

To refine our base regressions, we test whether certain factors are of special (or exclusive) importance for certain types of directors by adding

interaction variables. Specifically, we look at the interaction between several company-specific factors and the board members who are most likely to be viewed by investors as responsible for those factors. The existence of an interaction between a director's role or responsibility for a problem and the presence of that problem would suggest that proxy advisors are paying attention to relative accountability within the board. We test four specific interactions: (1) the interaction between audit committee membership and the presence of an audit-related problem such as an SEC investigation or a restatement; (2) the interaction between compensation committee membership and the presence of abnormally high levels of executive compensation; (3) the interaction between corporate performance and a director's status as CEO, employee director, or outside director; and (4) the interaction between service on a high number of boards and a director's status as CEO, employee director, or outside director.

Our hypothesis is that proxy advisors are more likely to issue withhold recommendations to target directors with specific responsibility for a problem. Thus, for the first two interactions, we expect the effect of a company problem to be focused on members of the relevant committee. We expect CEOs and employee directors to be more affected by corporate performance—receiving more withhold recommendations than the average director when the company underperforms and receiving fewer withhold recommendations when the company is doing well. As to membership on many boards, there are two opposing hypotheses. On one hand, if membership on other boards is a distraction, the effect is more likely to be important for CEOs and employee directors than for outside directors. On the other hand, if membership on other boards is related to one's success as CEO (or officer), and our performance variable controls for CEO success only imperfectly, CEO or employee director membership on many other boards could serve as a proxy for success, partially offsetting any adverse effect otherwise associated with such membership.

A. AUDITING PROBLEMS AND AUDIT COMMITTEE MEMBERSHIP

To examine the relationship between restatements or SEC investigations and audit committee membership, we ran the base logit model for a withhold recommendation with the addition of the variables $Prior\ Restat \times AuditMbr$ and $Prior\ SEC \times AuditMbr$.

Table 5 reports our results for the four proxy advisory firms' recommendations. In these regressions, $Prior\ Restat$ estimates the average

effect of a restatement on non-audit-committee members; the sum of *Prior Restat* and *Prior Restat* \times *AuditMbr* estimates the effect of a restatement on audit committee members; and the sum of *AuditMbr*, *Prior Restat*, and *Prior Restat* \times *AuditMbr* estimates the effect of being both an audit committee member and experiencing a restatement. The effects for *Prior SEC* are analogous.

In our base regressions, the audit/disclosure-related variables were consistently significant in the predicted direction only for GL. With the addition of interaction terms, the coefficient for restatements is no longer significant for GL, but the sum of *Prior Restat* and *Prior Restat* \times *AuditMbr* is significantly different from zero at the 1% level. This suggests that for GL, restatements affect the recommendations for audit committee members, but not for non-audit-committee members (the coefficient for *Prior Restat* alone is not significantly different from zero). As to prior SEC investigations, the results indicate that they affect both audit committee members and nonmembers, and we cannot reject the null hypothesis that there is no differential in the effect.

As to ISS and PG, audit/disclosure-related variables remain insignificant, as they were in the base regressions. For EJ, in the base regressions, a prior SEC investigation was associated with an *increased* likelihood of a withhold recommendation, but a restatement was associated with a *reduced* likelihood of a withhold recommendation. The addition of interaction terms indicates that the effect of an SEC investigation is confined to members of audit committees; the coefficient for *Prior SEC* is no longer significant, but the sum of *Prior SEC* and *Prior SEC* \times *AuditMbr* is significant at the 10% level. As to restatements, the results indicate that the apparent reduction in the likelihood of a withhold recommendation is confined to non-audit-committee members; the coefficient for *Prior Restat* is significant and negative, but the coefficient for *Prior Restat* \times *AuditMbr* is significant and positive, and the sum of *Prior Restat* and *Prior Restat* \times *AuditMbr* is not significantly different from zero, indicating no significant reduction in the likelihood of a withhold recommendation due to a restatement for audit committee members.

TABLE 5. Interaction Between *Prior Restat* and *Prior SEC* and *AuditMbr*; Interaction Between *Top5AbComp* and *CompMbr*

<i>Attribute</i>	<i>VoteISS</i>	<i>VotePG</i>	<i>VoteGL</i>	<i>VoteEJ</i>
<i>AuditMbr</i>	-0.104 (-0.88)	0.228 (1.13)	0.377*** (5.50)	0.129 (1.42)
<i>Prior Restat</i>	-0.381 (-1.48)	-1.015 (-1.44)	0.147 (1.03)	-0.640*** (-3.61)
<i>Prior Restat</i> × <i>AuditMbr</i>	0.277 (0.90)	0.531 (0.93)	0.554*** (2.88)	0.570* (2.23)
<i>Prior SEC</i>	0.164 (0.48)	1.069 (1.51)	0.361** (2.04)	0.159 (0.68)
<i>Prior SEC</i> × <i>AuditMbr</i>	0.233 (0.60)	-1.064 (-1.22)	-0.0673 (-0.33)	0.213 (0.70)
<i>CompMbr</i>	0.502*** (4.30)	1.675*** (4.33)	0.344*** (5.24)	0.432*** (4.85)
<i>Top5AbComp</i>	0.411 (0.89)	-0.567 (-0.51)	-0.0201 (-0.12)	0.436* (1.93)
<i>Top5AbComp</i> × <i>CompMbr</i>	0.481 (0.90)	3.374*** (2.89)	0.752*** (2.67)	-0.164 (-0.56)
<i>Year06</i>	-0.126 (-0.95)	0.165 (0.71)	0.148** (2.38)	-0.223*** (-3.06)
Constant	-3.426*** (-5.26)	-5.164*** (-3.43)	-1.948*** (-6.06)	-3.852*** (-8.16)
<i>N</i>	11,833	4509	12,973	11,809
pseudo <i>R</i> ²	0.153	0.216	0.108	0.207
Select F-Tests				
<i>Prior Restat</i> + <i>Prior Restat</i> × <i>AuditMbr</i>	0.7086	0.4721	0.0000	0.7404
<i>Prior Restat</i> + <i>AuditMbr</i> + <i>Prior Restat</i> × <i>AuditMbr</i>	0.4566	0.6995	0.0000	0.7867
<i>Prior SEC</i> + <i>Prior SEC</i> × <i>AuditMbr</i>	0.2434	0.9931	0.1034	0.0635
<i>Prior SEC</i> + <i>AuditMbr</i> + <i>Prior SEC</i> × <i>AuditMbr</i>	0.3887	0.7006	0.0003	0.0153
<i>Top5AbComp</i> + <i>Top5AbComp</i> × <i>CompMbr</i>	0.0275	0.0000	0.0033	0.1721
<i>Top5AbComp</i> + <i>CompMbr</i> + <i>Top5AbComp</i> × <i>CompMbr</i>	0.0007	0.0000	0.0000	0.0007

Note: *t*-statistics are in parentheses. F-tests are of the null hypothesis that the sum of the coefficients equals 0. All models use the base models in table 3 with the addition of interaction terms. We report only the coefficients for the additional interaction terms and associated variables.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

B. HIGH COMPENSATION AND COMPENSATION COMMITTEE MEMBERSHIP

To examine the relationship between top 5% abnormal compensation (*Top5AbComp*) and compensation committee membership (*CompMbr*), we also estimated the base logit model for a withhold recommendation with the addition of the interaction variable $Top5AbComp \times CompMbr$. Table 5 reports our results for the four proxy advisory firms' recommendations. *Top5AbComp* estimates the average effect of *Top5AbComp* on non-compensation-committee members, and the sum of *Top5AbComp* and $Top5AbComp \times CompMbr$ estimates the effect on compensation committee members (in each case relative to having the same position but not paying top compensation).

In the base logit models reported in table 3, paying abnormally high CEO compensation was associated with an increased likelihood of a withhold recommendation by ISS, PG, GL, and EJ. For GL and PG, the results of the logit models with interaction terms reported in table 5 indicate that paying abnormally high CEO compensation raises the likelihood of a withhold recommendation only for members of the compensation committee. The coefficient for *Top5AbComp* alone (measuring the effect of high CEO compensation for nonmembers) is insignificant; but the sum of *Top5AbComp* and $Top5AbComp \times CompMbr$ is positive and significant at the 1% level for each advisor. In the logit models with interaction terms, we obtain similar results for ISS, even though paying abnormally high compensation was insignificant for ISS in the base models. For EJ, by contrast, the regressions with interaction terms indicate that paying abnormally high CEO compensation is associated with a significant increase in the likelihood of a withhold recommendation for non-compensation-committee members (as measured by *Top5AbComp*). While $Top5AbComp + Top5AbComp \times CompMbr$ is positive, the sum is not significantly different from zero, and we thus cannot reject the hypothesis that paying abnormally high compensation has no effect on recommendations for compensation committee members.

C. PERFORMANCE AND INSIDE DIRECTORS

To examine the effect of performance on withhold recommendations for inside directors, we estimated the base logit models with the addition of the following variables: $Top5AbRet \times CEO$, $Top5AbRet \times Empl_Dir$, $Bot5AbRet \times CEO$, and $Bot5AbRet \times Empl_Dir$. Table 6 reports our results.

TABLE 6. Interaction Between *Top5AbRet* and *CEO* and *Empl_Dir*

Attribute	VoteISS	VotePG	VoteGL	VoteEJ
<i>CEO</i>	0.630*** (3.42)	-0.0755 (-0.18)	-1.064*** (-5.69)	-0.330 (-1.56)
<i>Empl_Dir</i>	1.487*** (6.05)	0.162 (0.17)	1.069*** (8.02)	0.345 (1.28)
<i>Top5AbRet</i>	-0.240 (-0.84)	-1.319* (-1.85)	-0.308 (-1.62)	-0.284 (-1.61)
<i>Top5AbRet</i> × <i>CEO</i>	0.495 (1.36)	...	0.752 (1.37)	0.626 (0.92)
<i>Top5AbRet</i> × <i>Empl_Dir</i>	0.905+ (1.67)	...	-0.0316 (-0.08)	0.890 (1.21)
<i>Bot5AbRet</i>	0.264 (0.88)	...	0.467*** (3.23)	0.126 (0.59)
<i>Bot5AbRet</i> × <i>CEO</i>	0.412 (0.95)	...	-1.502 (-1.48)	-0.341 (-0.31)
<i>Bot5AbRet</i> × <i>Empl_Dir</i>	0.614 (0.88)	...	-0.904* (-1.66)	0.411 (0.37)
<i>Year06</i>	-0.125 (-0.94)	0.162 (0.72)	0.144** (2.32)	-0.224*** (-3.07)
Constant	-3.430*** (-5.28)	-5.562*** (-3.75)	-2.002*** (-6.27)	-3.853*** (-8.22)
<i>N</i>	11,833	4468	12,973	11,809
pseudo <i>R</i> ²	0.153	0.197	0.107	0.207
Select F-Tests				
<i>Top5AbRet</i> + <i>Top5AbRet</i> × <i>CEO</i>	0.5985	...	0.4176	0.6028
<i>Top5AbRet</i> + <i>CEO</i> + <i>Top5AbRet</i> × <i>CEO</i>	0.0764	...	0.2401	0.9853
<i>Top5AbRet</i> + <i>Top5AbRet</i> × <i>Empl_Dir</i>	0.2384	...	0.3803	0.3865
<i>Top5AbRet</i> + <i>Empl_Dir</i> + <i>Top5AbRet</i> × <i>Empl_Dir</i>	0.0003	...	0.0611	0.1939
<i>Bot5AbRet</i> + <i>Bot5AbRet</i> × <i>CEO</i>	0.1492	...	0.3055	0.8425
<i>Bot5AbRet</i> + <i>CEO</i> + <i>Bot5AbRet</i> × <i>CEO</i>	0.0064	...	0.0363	0.6189
<i>Bot5AbRet</i> + <i>Bot5AbRet</i> × <i>Empl_Dir</i>	0.1992	...	0.4068	0.6282
<i>Bot5AbRet</i> + <i>Empl_Dir</i> + <i>Bot5AbRet</i> × <i>Empl_Dir</i>	0.0009	...	0.2368	0.4395

Note: *t*-statistics are in parentheses. F-tests are of the null hypothesis that the sum of the coefficients equals 0. All models use the base models in table 3 with the addition of interaction terms. We report only the coefficients for the additional interaction terms and associated variables. Where data are unavailable, ellipsis dots are inserted.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

In these regressions, *Top5AbRet* estimates the effect of top returns on directors who are neither the CEO nor employees of the company, and the sum of *Top5AbRet* and *Top5AbRet* \times *CEO* estimates the effect of top returns on the CEO. Effects for employee directors and bottom returns are analogous.

For ISS, as in the base logit models, the logit models with interactive terms produce no evidence that top or bottom returns affect ISS recommendations.

For GL, the logit models with interaction terms indicate that bottom returns affect the likelihood of a withhold recommendation only for outside directors (as measured by the *Bot5AbRet* variable). Contrary to our hypothesis, there is no evidence that bottom returns affect recommendations for inside directors (as measured by the sum of *Bot5AbRet* and *Bot5AbRet* \times *CEO*). The logit models also indicate that top returns do not affect the likelihood of a withhold recommendation for any director (as measured by *Top5AbRet* and the sums of *Top5AbRet* and *Top5AbRet* \times *CEO* and of *Top5AbRet* and *Top5AbRet* \times *Empl_Dir*).

For EJ, neither the base regressions nor the regressions with interactive terms generate evidence that our performance measures affect recommendations. For PG, we were unable to estimate the logit model with interaction terms because *Top5AbRet* \times *CEO* = 1, *Top5AbRet* \times *Empl_Dir* = 1, *Bot5AbRet* \times *CEO* = 1, and *Bot5AbRet* \times *Empl_Dir* = 1 were each perfectly correlated with a for recommendation by PG and, as a result, were dropped from the model.

D. MULTIPLE BOARD SEATS

To examine the effect of membership on many boards, we estimated the base logit models with the addition of the interaction variables *ManyBds* \times *CEO* and *ManyBds* \times *Empl_Dir*. Table 7 reports our results.

In these models, *ManyBds* estimates the effect of sitting on multiple boards on directors who are neither the CEO nor an employee of the company, and the sum of *ManyBds* and *ManyBds* \times *CEO* estimates the total effect of many board seats on the CEO. Effects for employee directors are analogous.

TABLE 7. Interaction Between *ManyBds* and *CEO* and *Empl_Dir*

<i>Attribute</i>	<i>VoteISS</i>	<i>VotePG</i>	<i>VoteGL</i>	<i>VoteEJ</i>
<i>CEO</i>	0.786*** (4.38)	-0.0300 (-0.07)	-1.111*** (-6.12)	-0.295 (-1.28)
<i>Empl_Dir</i>	1.615*** (6.63)	0.152 (0.15)	1.040*** (7.93)	0.480* (1.72)
<i>ManyBds</i>	0.903*** (6.44)	0.531* (1.82)	0.527*** (6.42)	2.440*** (24.45)
<i>ManyBds</i> × <i>CEO</i>	...	...	0.353 (0.52)	-0.0345 (-0.07)
<i>ManyBds</i> × <i>Empl_Dir</i>.	...	...	-0.327 (-0.36)	-1.276 (-1.60)
<i>Year06</i>	-0.130 (-0.98)	0.163 (0.72)	0.146** (2.34)	-0.225*** (-3.08)
Constant	-3.454*** (-5.32)	-5.560*** (-3.74)	-1.997*** (-6.26)	-3.860*** (-8.16)
<i>N</i>	11,777	4491	12,973	11,809
pseudo <i>R</i> ²	0.153	0.198	0.106	0.207
Select F-Tests				
<i>ManyBds</i> + <i>ManyBds</i> × <i>CEO</i>	...	...	0.1891	0.0000
<i>ManyBds</i> + <i>CEO</i> + <i>ManyBds</i> × <i>CEO</i>	...	...	0.7252	0.0000
<i>ManyBds</i> + <i>ManyBds</i> × <i>Empl_Dir</i>	...	...	0.8261	0.1392
<i>ManyBds</i> + <i>Empl_Dir</i> + <i>ManyBds</i> × <i>Empl_Dir</i>	...	...	0.1741	0.0384

Note: *t*-statistics are in parentheses. F-tests are of the null hypothesis that the sum of the coefficients equals 0. All models use the base models in table 3 with the addition of interaction terms. We report only the coefficients for the additional interaction terms and associated variables. Where data are unavailable, ellipsis dots are inserted.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

In the base logit models reported in table 3, sitting on multiple boards increased the likelihood of a withhold recommendation for GL and EJ. The logit models with interaction terms reported in table 7 suggest that, in the case of GL, this effect may be confined to outside directors. For outside directors, sitting on multiple boards is associated with a higher likelihood of a withhold recommendation for non-CEOs (at the 1% level), as measured by the coefficient for *ManyBds* alone. By contrast, neither *ManyBds* + *ManyBds* × *Empl_Dir* (for GL and EJ) nor *ManyBds* + *ManyBds* × *CEO* (for GL) is significantly different from zero.

For EJ, both *ManyBds* alone and *Many Bds* + *ManyBds* × *CEO* are highly significant, and the sum of *ManyBds* and *ManyBds* × *Empl_Dir* is borderline insignificant. For ISS and PG, we were unable to estimate the logit model with interaction terms because, for both, *ManyBds* × *Empl_Dir*

$= 1$ and $ManyBds \times CEO = 1$ were perfectly correlated with a for recommendation and, as a result, were dropped from the model.

E. SUMMARY

Overall, the set of regressions with interaction variables indicates that, at least in the case of some advisors, members of the relevant committee are held particularly responsible for problems within that committee's jurisdiction. Thus, we find that for ISS, PG, and GL, the adverse effects of high compensation are focused on compensation committee members; for GL, the adverse effects of a restatement are felt by audit committee members; for EJ, the adverse effects of an SEC investigation are tied to audit committee members; for ISS, the adverse effects of bottom returns are confined to CEOs; and for GL, the adverse effects of sitting on multiple boards relate only to outside directors.

V. MULTIPLE NOMINATIONS

A large number of individuals in our sample were nominated for election to the boards of several companies in the same year and received multiple recommendations by the same proxy advisor, as reported in table 8.1. For these sets of nominees, we investigated the relationship between the multiple recommendations for the same person made by each advisor.

As a starting point, we examined whether the overall withhold percentage for directors who received multiple recommendations from a proxy advisor differs from the withhold percentage for directors who received only a single recommendation from the same proxy advisor. Note that the number of recommendations from a proxy advisor is correlated with, but not identical to, the number of board seats because (1) the director may sit on a staggered board of a different company that does not have an election in that year or (2) even if the other company has an election in the same year, the proxy advisor may not issue a recommendation because its coverage is less than 100 percent. Table 8.2 provides the withhold percentages for each advisor depending on whether the individual received one, two, or three recommendations from that advisor.⁷² Except for EJ, the differences in withhold percentages are statistically (and, for the most part, economically) insignificant.

72. ISS, GL, and EJ had some individuals who received more than three recommendations, but those numbers of individuals were too small for statistical analysis.

TABLE 8.1. Number of Individuals with Multiple Nominations

ISS	1547
PG	295
GL	1792
EJ	1638

TABLE 8.2. Withhold Percentages for Nominees

<i>N</i>	<i>ISS</i>	<i>PG</i>	<i>GL</i>	<i>EJ</i>
1	0.067565	0.035389	0.187367	0.079342
2	0.056641	0.048214	0.176570	0.144131 ^a
3	0.070175	0.088889	0.217662	0.305785 ^b

Note: *N* is the number of boards for which an individual received a recommendation by an advisor. For EJ, ^a indicates the *t*-test of the difference in withhold percentage for *N* = 2 versus *N* = 1 is significant at the 1% level; ^b indicates the *t*-test of the difference in withhold percentage for *N* = 3 versus *N* = 1 is significant at the 1% level.

TABLE 8.3. Conditional Probabilities

<i>N</i>	<i>Calculation</i>	<i>ISS</i>	<i>PG</i>	<i>GL</i>	<i>EJ</i>
2	P(W/H, F)	4.8	4.3	16.6	8.9
2	P(W/H, W/H)	19.3	14.8	22.6	47.0
3	P(W/H-W/H, F)	1.4		3.7	4.8
3	P(W/H-W/H, W/H)	12.5		24.0	64.9
3	P(W/H-*, F)	8.9		31.3	16.7
3	P(W/H-*, W/H)	50.0		50.3	86.5
3	P(W/H-F, F)	7.5		27.6	11.9
3	P(W/H-F, W/H)	37.5		26.7	21.6

Note: *N* is the number of boards for which an individual received a recommendation by an advisor. "P(W/H, F)" and "P(W/H, W/H)" are, respectively, the conditional probabilities of a withhold recommendation conditional (for nominees with 2 recommendations) on the other recommendation being for or withhold. "P(W/H-W/H, F)" and "P(W/H-W/H, W/H)" are, respectively, the conditional probabilities of two withhold recommendations conditional (for nominees with 3 recommendations) on the other recommendation being for or withhold. "P(W/H-*, F)" and "P(W/H-*, W/H)" are, respectively, the conditional probabilities of at least one withhold recommendation conditional (for nominees with 3 recommendations) on the other recommendation being for or withhold. "P(W/H-F, F)" and "P(W/H-F, W/H)" are, respectively, the conditional probabilities of exactly one withhold recommendation conditional (for nominees with 3 recommendations) on the other recommendation being for or withhold.

We next turn to whether recommendations for the same individual from the same advisor are correlated. Our null hypothesis is that recommendations are not correlated. To test this hypothesis, we calculated the following: for individuals who received two recommendations (*i*, *j*), we calculated the conditional probabilities for each advisor that *i* = withhold, conditional on *j* = for and on *j* = withhold; for individuals who received three recommendations (*i*, *j*, *k*), we calculated the conditional probabilities for each advisor (other than PG, which had too few observations) that both *i* = withhold and *j* = withhold, or that either *i* = withhold or *j* = withhold, conditional on *k* = for and on *k* = withhold. The results are reported in table 8.3.

For each of the advisors, we can reject the null hypothesis that the recommendations are independent. Note, however, that the degree of

correlation in the recommendations differs substantially among advisors. Generally, the correlation is strongest for EJ and weakest for GL, with ISS and PG occupying an intermediate position. For EJ, for example, the conditional probability of a withhold recommendation for a double-nomination individual increases from 9% to 47% depending on whether the other recommendation is for or withhold. For GL, that increase is much more modest, from 17% to 23%; for ISS and PG, it is, respectively, from 5% to 19% and from 4% to 15%.

Three reasons may account for the correlation among recommendations. First, there may be a spillover effect in that the proxy advisor will take into account the conduct that led to a withhold recommendation for board 1 in issuing its recommendation for board 2 (the “spillover hypothesis”). Second, the same factor (for example, a criminal conviction), which is not tied to service on a particular board, may account for multiple withhold recommendations (the “single factor hypothesis”). Third, certain individuals may be more likely to engage in conduct (for example, because they are lazy) that results in a withhold recommendation (the “higher proclivity hypothesis”). For these individuals, the ex ante likelihood of a withhold recommendation is higher than for others. Although, given this higher ex ante likelihood, each recommendation is independent, the recommendations are correlated when they are pooled with individuals who have a lower ex ante likelihood of a withhold recommendation.

To differentiate between these hypotheses, the following test was performed. The spillover hypothesis suggests that the order in which the conduct of directors is assessed matters. Conduct on board 1 that results in a withhold recommendation should result in a withhold recommendation for board 2 only if that conduct has been evaluated by the time the recommendation for board 2 is released. Proxy advisors, of course, do not release all recommendations at the same time but generally release each recommendation shortly before the corresponding annual meeting. The dates of the annual meetings should thus provide a rough benchmark of the timing of the proxy advisor’s evaluation. The spillover hypothesis would thus suggest that a withhold recommendation for board 1 should be correlated with a withhold recommendation for board 2 only if the annual meeting for board 1 preceded the meeting for board 2. The data, however, provide no support for the spillover hypothesis for any of the proxy advisors. In each case, the order of the meetings had no effect on

correlations.⁷³

To differentiate between the single factor and the higher proclivity hypothesis, we focused on individuals who received three recommendations by a single advisor. The single factor hypothesis would predict that, if one of these recommendations is withhold, the likelihood of both of the other recommendations being withhold should increase substantially, but there should be no increase in the likelihood that one of the other two (but *not* both) is withhold. The higher proclivity hypothesis would predict a lesser increase in the former likelihood but an increase in the latter.

The data indicate strong support for the single factor hypothesis with respect to GL. If one recommendation is withhold rather than for, the likelihood that both other recommendations are also withhold increases from 4% to 24%; but the likelihood that only one (but not both) of them is withhold stays roughly the same (27.6% versus 26.7%).

For ISS, by contrast, the data support the higher proclivity hypothesis. If one recommendation is withhold, the likelihood of getting a single other withhold increases from 8% to 38%. The likelihood of getting two withholds, of course, also increases (from 1.4% to 12.5%), but that increase is in line with the increase that would be expected given a higher proclivity to get a withhold recommendation.

For EJ, in turn, the data support both hypotheses. The likelihood of getting a single other withhold increases from 12% to 22%, showing support for the higher proclivity hypothesis, and the likelihood of getting two withholds increases from 5% to 65%, which is more than what one would expect if only the higher proclivity hypothesis were correct.

On the whole, therefore, the data indicate significant differences in the manner in which, and the reasons why, recommendations for the same individual are correlated. For GL, the correlation is driven predominantly by the same factors that, when present, result in across-the-board withhold recommendations. For ISS, the correlation is likely due to the fact that some individuals are more prone to take (or refrain from taking) actions that result in a withhold recommendation. Given this trait, however, recommendations are independent. For EJ, it is likely that both of these forces are at work for different individuals. For none of the advisors did we

73. In particular, the spillover hypothesis would predict that, for advisors who issued two recommendations, there would be fewer withhold/for recommendations (in that chronological order) than for/withhold recommendations. For all advisors, these numbers were virtually identical.

find evidence that they consider a director's conduct on one board in issuing a recommendation for a different board.

To further investigate the reasons why some directors receive across-the-board withhold recommendations, we compared, for each proxy advisor, the characteristics of nominees who received all withhold recommendations (the "all withhold" group) and those who received at least one withhold recommendation but at least one other for recommendation (the "mixed withhold" group). For ISS and PG, the former group was too small to make meaningful comparisons.

For GL, we found that nominees who sat on more than the median number of boards, and those who were members of audit committees, were much more prevalent in the all withhold group than in the mixed withhold group (55% versus 35% for members of many boards, 60% versus 46% for audit committee members), but members of compensation committees were less prevalent in the all withhold group than in the mixed withhold group (38% versus 55%). One plausible explanation is that membership on too many boards, and certain conduct on the part of audit committee members (or membership on too many audit committees), lead to across-the-board withhold recommendations for GL.

For EJ, we also found that nominees who sat on more than the median number of boards were more prevalent in the all withhold group than in the mixed withhold group (81% versus 51%). In addition, members of compensation committees were somewhat more prevalent in the all withhold group (54% versus 46%), but outside linked directors were substantially less prevalent in the all withhold group than in the mixed withhold group (7% versus 24%). Again, a plausible explanation is that membership on too many boards, and possibly certain conduct on the part of compensation committee members, lead to across-the-board withhold recommendations for EJ. As to why outside linked directors are relatively uncommon in the all withhold group, the likely explanation is that the factors associated with across-the-board withhold recommendations are negatively correlated with being an outside linked director.

VI. GROUP-BASED RECOMMENDATIONS AND INTRACOMPANY SPILLOVER RECOMMENDATIONS

We next examined how the recommendations for nominees to the board of a single company relate to each other. To do this, we examined, for each advisor, those recommendations where the advisor issued recommendations (either for or withhold) for at least six nominees to the

same board. We further divided these recommendation samples into three subsets: recommendation subsamples where the fraction of withhold recommendations for nominees to the same board was less than 0.34 (the “low-withhold” subsample); those where that fraction was greater than 0.34 but less than 0.66 (the “medium-withhold” subsample); and those where that fraction was greater than 0.66 (the “high-withhold” subsample). High-withhold situations thus occur when a proxy advisor issues a withhold recommendation for a substantial (more than two-thirds) fraction of the board. Low-withhold situations occur when a proxy advisor focuses its withhold recommendation on one or a small number of directors on a specific board.

Table 9.1 provides, for each proxy advisor, the number of withhold recommendations in each subsample. Table 9.1 shows that the percentages of withhold recommendations in each subsample (as the percentage of all withhold recommendations) are not equally distributed for each proxy advisor. Specifically, for ISS and PG, a much greater proportion of all withhold recommendations are in the medium- and high-withhold subsamples than for GL and EJ. Notably, one would expect that advisors that are generally more likely to issue withhold recommendations would have a higher proportion of their withhold recommendations in the medium- and high- withhold subsamples. However, ISS and PG are generally less likely to issue withhold recommendations than GL and EJ.

To take direct account of the differences in the overall withhold rate, we calculated, based on the actual distribution of board sizes in each subsample, the expected number of withhold recommendations, in each subsample and for each advisor, given the overall rate of withhold recommendations for that advisor and assuming that recommendations for each nominee are independent. Comparing the expected and actual number of withhold recommendations shows that, for each advisor, the number of actual withhold recommendations in the medium- and high-withhold subsamples is higher than expected, given the assumption that recommendations are independent. This suggests that withhold recommendations among nominees for the same board by the same advisor are positively correlated.

TABLE 9.1. Withhold Subsamples

	<i>Low- Withhold</i>	<i>Medium- Withhold</i>	<i>High- Withhold</i>	<i>Total Withhold</i>
ISS Actual Number of W/H Recs. in Subsample	250	180	126	556
ISS % of Total W/H Recs.	45%	32%	23%	100%
ISS Expected Number of W/H Recs.	543.3	12.6	0.1	556
PG Actual Number of W/H Recs. in Subsample	43	83	8	134
PG % of Total W/H Recs.	32%	62%	6%	100%
PG Expected Number of W/H Recs.	132.9	1.0	0.0	134
GL Actual Number of W/H Recs. in Subsample	1061	713	147	1921
GL % of Total W/H Recs.	55%	37%	8%	100%
GL Expected Number of W/H Recs.	1471.3	436.1	13.7	1921
EJ Actual Number of W/H Recs. in Subsample	834	267	16	1117
EJ % of Total W/H Recs.	75%	24%	1%	100%
EJ Expected Number of W/H Recs.	1014.8	100.6	1.6	1117

The degree to which the number of withhold recommendations in the medium and high groups exceeds the expected number differs substantially among advisors. For GL and EJ, the number of actual withhold recommendations in the medium and high subsamples combined is, respectively, 1.9 and 2.8 times the expected number. By contrast, for ISS and PG, the number of actual withhold recommendations in the medium and high groups is, respectively, 24.1 and 91.0 times the expected number. This indicates that the positive correlation of recommendations among nominees to the same board is higher for ISS and PG than for GL and EJ.

Two factors can generate a positive correlation in recommendations among nominees to the board. First, the proxy advisor may issue “group-based” recommendations. For example, the advisor may issue withhold recommendations for the whole compensation committee (or even the whole board) if it finds that the CEO is receiving excessive compensation. Second, the advisor may issue “spillover” recommendations, where attributes of one nominee affect the recommendation of other nominees. For example, a proxy advisor may not generally issue withhold recommendations for outside linked directors if the total number of such nominees to the board of a single company is sufficiently low, but may

TABLE 9.2. Attribute Representation in ISS and PG Withhold Subsamples

<i>Attribute</i>	<i>ISS Low</i>	<i>ISS Medium</i>	<i>ISS High</i>	<i>PG Low</i>	<i>PG Medium</i>
<i>CEO</i>	2.7%	15.0%	11.8%	0.0%	1.2%
<i>New Director</i>	15.0%	8.9%	7.9%	2.3%	3.6%
<i>AuditMbr</i>	28.7%	13.9%	38.2%	39.4%	47.6%
<i>Prior Restat</i>	12.4%	7.2%	3.2%	9.3%	3.6%
<i>Prior SEC</i>	10.4%	10.0%	8.7%	4.7%	14.5%
<i>CompMbr</i>	50.2%	27.7%	44.6%	81.8%	93.9%
<i>Top5AbComp</i>	7.5%	17.8%	8.9%	16.3%	30.3%
<i>Attendance</i>	9.0%	1.2%	0.0%	9.1%	2.4%
<i>ManyBds</i>	27.6%	5.1%	10.4%	18.2%	6.1%
<i>Age75</i>	16.0%	12.8%	16.7%	23.3%	16.7%
<i>NomMbr</i>	57.0%	21.2%	35.5%	48.5%	46.3%
<i>Empl_Dir</i>	3.1%	31.3%	6.4%	0.0%	0.0%
<i>OutDirLink</i>	48.0%	28.3%	18.2%	12.1%	7.3%
<i>BlockDir</i>	1.8%	8.4%	2.7%	0.0%	0.0%
<i>IP No</i>	0.0%	0.0%	17.8%	0.0%	0.0%
<i>Bot5AbRet</i>	6.8%	0.0%	4.8%	0.0%	0.0%
<i>Top5AbRet</i>	6.4%	6.7%	9.5%	7.0%	3.6%

Note: Numbers are the percentages of the withhold recommendations for the particular subsample. For example, directors with the *IP No* attribute account for 17.8% of the ISS withhold recommendations that resulted in the high category.

issue withhold recommendations for *all* outside linked director nominees if too many of them are nominated to the same board. Correlations may be higher for those proxy advisors that employ group-based or spillover recommendations relatively more frequently.

To determine what accounts for the high positive correlation among nominees in recommendations made by ISS and PG, we compared the nominees who received withhold recommendations in the low-withhold subsample to those who received withhold recommendations in the medium-withhold and high-withhold subsamples. (Given the low number of withhold recommendations in the PG high-withhold group, we did not include figures for that subsample.) In the absence of group-based and spillover recommendations, we would expect no systematic difference in these attributes. The data are presented in table 9.2.

For ISS, we find that CEOs account for a significantly greater percentage of the withhold recommendations in the medium-withhold group than in the low-withhold group. Similarly, employee directors and

block directors are more highly represented in the medium- (and, to a lesser extent, in the high-) withhold group than in the low-withhold group. In contrast to these insider and quasi-insider directors, members of audit, compensation or nominating committees (which consist predominantly of outside directors) and outside linked directors are relatively underrepresented in the medium-withhold group. This suggests a possible spillover effect that we investigate further below.

In addition, table 9.2 provides evidence that ISS issues group-based withhold recommendations (covering all or almost all nominees) when it determines that the board has inappropriately ignored a shareholder proposal. Such nominees account for 17.8% of the withhold recommendations in the high withhold group, but none in the low- and medium-withhold groups. Notably, GL, the only other advisor for which *IP No* was statistically significant, does not make it a basis for group-based withhold recommendations. Nominees coded as *IP No* account for 0.9% of the withhold recommendations in the low group and, respectively, 1.1% and 0.0% of the withhold recommendations in the medium and high groups.

Consistent with our earlier finding that paying abnormally high compensation is associated with an increased likelihood of a withhold recommendation for compensation committee members (but not for other directors), we also find that *Top5AbComp* accounts for a higher percentage of the withhold recommendations in the medium group than in the other groups.

For PG, the most salient result is that withhold recommendations in the medium-withhold group consist disproportionately of nominees on boards where the CEO receives abnormally high compensation compared with the low-withhold group (30.3% of the withhold recommendations in the medium group versus 16.3% in the low-withhold group) and almost entirely of members of the compensation committee (93.9%, or seventy-seven of eighty-two nominees that received withhold recommendations, in the medium group versus 81.8% in the low-withhold group). Conversely (and not reported in table 9.2), only two of seventy-nine compensation committee members in the medium-withhold subsample received a for recommendation. This evidence indicates that PG issues group-based recommendations on compensation committee members for compensation issues (but not for any other directors and other issues), holding the entire committee responsible for inappropriate compensation practices.

We now turn to examining more closely our earlier finding that, as to ISS, CEOs, as well as employee directors and block directors, are more highly represented in the medium-withhold group than in the low-withhold group. This finding is of special interest because ISS is reported to be the most influential proxy advisor and because it is the only advisor for which being a CEO is associated with an increased likelihood of a withhold recommendation (see table 3 above). The data in table 9.2 suggest that this association is attributable to group-based or spillover effects, since CEOs are substantially underrepresented in the low-withhold subsample.

We hypothesize that withhold recommendations for CEOs in the medium-withhold subsample represent a spillover effect from the presence of excessive numbers of “suspect” directors on the board. When ISS considers that number to be inappropriately high, it issues withhold recommendations for both the suspect directors and the CEO, with the result that CEOs are overrepresented in the medium-withhold subsample.⁷⁴

For the purpose of our hypothesis, we consider three types of directors as potentially suspect: employee directors, outside linked directors, and block directors. Note that employee and block directors are themselves overrepresented in the medium-withhold subsample. This may be due to a spillover effect—that is, ISS may be more likely to issue withhold recommendations for these types of suspect directors when their number is inappropriately high. By contrast, outside linked directors are more highly represented in the low-withhold subsample than in the medium-withhold subsample. This suggests that ISS tends to issue withhold recommendations for outside linked directors regardless of their number (that is, without any spillover effect). Indeed, as shown in table 9.3, outside linked directors account for 9.9% of all nominees (who received either a for or a withhold recommendation) in the low-withhold subsample; but they account for 43% of nominees who received a withhold recommendation in the low-withhold subsample. Thus, even in that subsample, being an outside linked director is associated with an increased likelihood of an ISS withhold recommendation. By contrast, being a CEO or employee director is not associated with an increased likelihood of a withhold recommendation in the low-withhold subsample. (As shown in table 9.3, CEOs and employee directors are less frequently represented among nominees who received withhold recommendations than among nominees overall in the low-withhold subsample.)

74. In effect, ISS may be holding the CEO responsible for allowing the issuer to maintain an ineffective board or lobbying for the CEO's replacement in circumstances in which the board is unresponsive.

TABLE 9.3. Types of Directors in ISS Withhold Subsamples

<i>Attribute</i>	<i>Low Subsample: All Recs.</i>	<i>Low Subsample: W/H Recs. Only</i>	<i>Med. Subsample: All Recs.</i>	<i>Med. Subsample: W/H Recs. Only</i>
All Nominees	8434	250	361	180
<i>CEO</i>	840 (10.0%)	6 (2.4%)	35 (9.7%)	25 (13.9%)
<i>Empl_Dir</i>	496 (5.9%)	7 (2.8%)	57 (15.8%)	52 (28.9%)
<i>OutLinkDir</i>	834 (9.9%)	107 (42.8%)	57 (15.8%)	47 (26.1%)
<i>BlockDir</i>	57 (0.6%)	4 (1.6%)	15 (4.2%)	14 (7.8%)

Note: Percentages of all nominees are in parentheses.

Even if ISS issues withhold recommendations for outside linked directors regardless of their number, the number of outside linked directors may affect the likelihood that other types of directors, specifically CEOs, receive a withhold recommendation. Note, in this respect, that outside linked directors account for a higher proportion of all nominees for medium-withhold boards than they do for all nominees for low-withhold boards. This indicates that the number of outside linked directors on a board may be related to the percentage of nominees who received withhold recommendations.

To test for the presence of spillover effects, we repeat our base regression with several additions. First, we add dummy variables for the presence of various types of potentially suspect directors as follows: *Many_Empl_Dir*, taking the value of 1 if the number of employee director nominees is two or more and 0 otherwise; *Many_OutDirLink*, taking the value of 1 if the number of outside linked director nominees is two or more and 0 otherwise; and *Many_BlockDir*, taking the value of 1 if the number of block director nominees is one or more and 0 otherwise. We then interact each of these dummy variables with *CEO* and further interact *Many_Empl_Dir* with *Empl_Dir*, *Many_OutDirLink* with *OutDirLink*, and *Many_BlockDir* with *BlockDir* (the latter variable being collinear with *BlockDir*). The results of this regression are presented in table 10. (For simplicity, we report only the results for the added variables as well as for *CEO*, *Empl_Dir*, and *OutDirLink*.)

TABLE 10. Suspect Directors

<i>Attribute</i>	<i>VoteISS</i>	<i>VotePG</i>	<i>VoteGL</i>	<i>VoteEJ</i>
<i>CEO</i>	0.242 (1.18)	-0.856 [*] (-1.88)	-1.183 ^{***} (-5.87)	-0.607 ^{**} (-2.37)
<i>Empl_Dir</i>	1.172 ^{***} (4.26)	0.750 (0.71)	0.882 ^{***} (5.10)	-0.101 (-0.31)
<i>Many_Empl_Dir</i>	0.0573 (0.23)	0.473 (0.64)	0.223 [*] (1.82)	-0.139 (-0.86)
<i>Many_Empl_Dir</i> × <i>Empl_Dir</i>	0.838 ^{**} (2.20)	...	0.173 (0.83)	1.145 ^{**} (2.35)
<i>Many_Empl_Dir</i> × <i>CEO</i>	1.212 ^{***} (3.20)	...	-1.383 [*] (-1.83)	0.819 (1.44)
<i>OutDirLink</i>	1.895 ^{***} (10.64)	0.654 (1.43)	1.401 ^{***} (12.69)	1.663 ^{***} (11.50)
<i>Many_OutDirLink</i>	0.139 (0.56)	0.705 (1.57)	0.023 (0.24)	0.122 (0.91)
<i>Many_OutDirLink</i> × <i>OutDirLink</i>	0.083 (0.33)	-1.050 (-0.89)	0.030 (0.18)	0.313 (1.57)
<i>Many_OutDirLink</i> × <i>CEO</i>	0.606 ^{**} (2.11)	0.533 (0.37)	0.312 (0.73)	0.213 (0.47)
<i>BlockDir</i>	0.180 (0.63)	2.622 ^{***} (3.21)	0.439 (1.58)	0.830 ^{**} (2.34)
<i>Many_BlockDir</i>	0.593 ^{**} (1.96)	-1.402 (-1.48)	-0.003 (-0.02)	0.424 [*] (1.89)
<i>Many_BlockDir</i> × <i>CEO</i>	1.066 ^{***} (3.94)	3.045 ^{***} (3.15)	1.125 ^{**} (2.25)	1.200 ^{**} (2.49)
<i>Year06</i>	-0.134 (-1.02)	0.189 (0.82)	0.148 ^{**} (2.39)	-0.215 ^{***} (-2.94)
Constant	-3.876 ^{***} (-5.93)	-5.883 ^{***} (-3.67)	-2.083 ^{***} (-6.42)	-4.110 ^{***} (-8.58)
<i>N</i>	11,833	4388	12,973	11,809
pseudo <i>R</i> ²	0.163	0.212	0.108	0.211

Note: *t*-statistics are in parentheses. All models use the base model in table 3 with the addition of interaction terms. We report only the coefficients for the additional interaction terms and associated variables. Where data are unavailable, ellipsis dots are inserted.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

The results for ISS indicate a substantial spillover effect of all three classifications of potentially suspect directors onto CEO. The presence of any type of suspect director nominee significantly increases the likelihood of an ISS withhold recommendation for the CEO. (In F-tests, *Many_Empl_Dir* + *Many_Empl_Dir* × *CEO*, *Many_OutDirLink* + *Many_OutDirLink* × *CEO*, and *Many_BlockDir* + *Many_BlockDir* × *CEO* are significant at the 1%, 5%, and 1% levels, respectively; *CEO* + *Empl_Dir* + *Many_Empl_Dir* × *CEO*, *CEO* + *Many_OutDirLink* +

$Many_OutDirLink \times CEO$, and $CEO + Many_BlockDir + Many_BlockDir \times CEO$ are each significant at the 1% level.) In the absence of these spillover factors, CEOs do not have an increased likelihood of receiving a withhold recommendation (the CEO variable on its own is insignificant). Thus, the finding in our base regression that CEOs are significantly more likely to receive an ISS withhold recommendation is entirely explained by spillover effects. Our results are robust for various variations, such as excluding nominees from companies with classified boards, adding additional interaction variables, and using different variables to signify an excessive number of suspect directors. We also find evidence that the likelihood of a withhold recommendation for employee directors increases if there are at least two employee directors nominated to the board (in F-tests, $Many_Empl_Dir + Many_Empl_Dir \times Empl_Dir$ is significant at the 5% level).

We run similar regressions for the other proxy advisors. We find no evidence of any spillover effects for PG. For GL, we find weak evidence that the likelihood of a withhold recommendation for any nominee (other than the CEO) increases if there are at least two employee directors nominated to the board ($Many_Empl_Dir$ is significant, but only at the 10% level). Furthermore, we find that, while CEOs are generally less likely to receive a withhold recommendation from GL, they are no less likely to receive a withhold recommendation if at least one block director is nominated to the board ($CEO + Many_BlockDir + Many_BlockDir \times CEO$ is insignificant). For EJ, we find that employee directors are significantly more likely to receive a withhold recommendation if and only if at least two such directors are nominated ($Empl_Dir$ is insignificant, while $Empl_Dir + Many_Empl_Dir + Many_Empl_Dir \times Empl_Dir$ is significant at the 5% level); that outside linked directors are more likely (at the 5% level) to receive a withhold recommendation if at least two such directors are nominated; and that CEOs, who are ordinarily less likely to receive a withhold recommendation, are more likely (at the 10% level) to do so if at least one block director is nominated to the board.

The results of these analyses suggest that ISS (and to a lesser degree GL and EJ) considers the overall composition of the board as an important factor in issuing recommendations on specific directors. Combining this finding with the results of the previous sections indicates that proxy advisors may focus their evaluation of a particular nominee primarily within the context of a specific company.

VII. IMPLICATIONS AND CONCLUSIONS

Our analysis largely supports the conclusion that proxy advisors provide a valuable service to their investor clients. Significantly, advisor recommendations—at least with respect to uncontested director elections—appear to be based on the factors that should matter to investors: good governance, director attention, and performance. We find compelling evidence that withhold recommendations are made in response to identifiable issuer- and director-specific problems, including, among others, financial restatements, SEC investigations, excessive executive compensation, failure to attend board meetings, lack of independence, and failure to implement precatory proposals adopted by shareholders. By contrast, antitakeover devices, which are often the subject of precatory shareholder resolutions, appear to have no impact on recommendations in director elections.

We find mixed evidence (depending on the advisor and the issue) that advisors use withhold recommendations to target those board members who bear responsibility for the issuer-specific problems triggering the recommendations. Of particular interest may be our findings that only one proxy advisor (ISS) is more likely to issue a withhold recommendation for the CEO if the company's stock price persistently underperforms the market averages and that no advisor is less likely to issue a withhold recommendation for the CEO if the company's stock price consistently outperforms the market averages.

Among our most significant findings about proxy advisor recommendations is the heterogeneity among proxy advisors. Proxy advisors differ significantly from each other in their propensity to issue withhold recommendations, in the factors on which they base their recommendations, in the weight accorded to those factors, in their propensity to issue a greater number of withhold recommendations for persons nominated for multiple board seats, in their proclivity to issue group-based and spillover recommendations, and in their reasons for doing so.

This heterogeneity raises the initial issue of whether and to what extent the institutional investors who hire these proxy advisors are aware of the factors each advisor uses in making its recommendations. To the extent that investors are aware of those factors or will become so (as a result of this or similar studies), heterogeneity is desirable as it enables investors to subscribe to and follow the recommendations of those advisors that conform to the investor's assessment of value-maximizing corporate

governance. For example, an investor who believes that proper audit and disclosure is the most important board function may be best served by following the recommendations of GL, while an investor concerned with executive compensation may want to give serious weight to recommendations by PG. Moreover, public examination of the factors that result in withhold recommendations increases transparency and makes proxy advisors (and those institutional investors that follow their recommendations) more accountable to members of the public who hold shares through institutional investors and to corporate governance policymakers.

To the extent that investors are not aware of these factors, however, the fact that the different advisors employ substantially different methodologies in making recommendations suggests that investors may not accurately perceive the information content associated with a withhold recommendation. This could lead investors to follow blindly the recommendation of a proxy advisor, even when that recommendation is based on factors that the investors would not consider relevant. In that case, proxy advisors would not be serving the goal of facilitating an informed shareholder vote. The result would be to reduce the effectiveness of the shareholder franchise because shareholders would not be voting their true preferences. In such a scenario, proposals to expand the shareholder vote should be taken up with caution. Likewise, the criticism of proxy advisors—as powerful governance actors that lack proper incentives and accountability as to the content of their recommendations and have the ability to base these recommendations on their whim, to follow their own ideological agenda, or perhaps even to pursue their own conflicting business interests—would warrant serious attention.

APPENDIX. Variable Definitions

Variable	Definition
<i>Age75</i>	Indicator variable equal to 1 if the director is seventy-five years old or older and 0 otherwise.
<i>Attendance</i>	Indicator variable equal to 1 if the director attended less than 75 percent of the meetings (as tracked by the IRRC for the year prior to the annual meeting date) and 0 otherwise.
<i>AuditMbr</i>	Indicator variable equal to 1 if the director is a member of the audit committee and 0 otherwise.
<i>BlockDir</i>	Indicator variable equal to 1 if the director owns more than 20 percent of the outstanding shares of the company in question and 0 otherwise.
<i>Bot5AbRet</i>	Indicator variable equal to 1 if the abnormal return for the three-year period prior to the annual meeting date for the company in question is in the bottom 5 percent of the sample and 0 otherwise. The abnormal return is defined as the difference between the raw three-year holding period return for the company in question and the three-year holding period return for the CRSP value-weighted market index.
<i>CEO</i>	Indicator variable equal to 1 if the director is the CEO of the company in question and 0 otherwise.
<i>Chairman Only</i>	Indicator variable equal to 1 if the director is the chairman of the board of the company in question (but not an employee) and 0 otherwise.
<i>ClassBd</i>	Indicator variable equal to 1 if the director sits on a classified board for the company in question (as measured by the IRRC for the year prior to the annual meeting date) and 0 otherwise.
<i>CompMbr</i>	Indicator variable equal to 1 if the director is a member of the compensation committee and 0 otherwise.
<i>CumVote</i>	Indicator variable equal to 1 if the company in question uses cumulative voting to elect directors (as measured by the IRRC for the year prior to the annual meeting date) and 0 otherwise.
<i>Empl_Dir</i>	Indicator variable equal to 1 if the director is an employee of the company in question (but not the CEO) and 0 otherwise.

<i>GP</i>	Indicator variable equal to 1 if the company in question uses golden parachute agreements (as measured by the IRRC for the year prior to the annual meeting date) and 0 otherwise.
<i>Interlock</i>	Indicator variable equal to 1 if the director met the IRRC criteria for an interlocking director in the year prior to the annual meeting date and 0 otherwise. The IRRC defines an interlocking directorship as follows: a directorship “whereby a director and executive of the company ABC sits on a board of another company XYZ and a director and executive of company XYZ sits on the board of company ABC that has an executive and director who also sit[s] on the original company’s board.” Definitions for RiskMetrics’ Directors Dataset, http://wrds.wharton.upenn.edu/ds/riskmetrics/dir_doc.shtml (last visited Apr. 20, 2009).
<i>IP No</i>	Indicator variable equal to 1 if the company in question faced a proxy issue proposal that received a majority for vote and failed to implement the recommendations of the proxy issue proposal within the following year and 0 otherwise.
<i>ManyBds</i>	Indicator variable equal to 1 if the director is a member of at least three other “major” company boards (as followed by the IRRC for the year prior to the annual meeting date) and 0 otherwise.
<i>New Director</i>	Indicator variable equal to 1 if the director has been on the board for less than two years.
<i>NomMbr</i>	Indicator variable equal to 1 if the director is a member of the nominating committee and 0 otherwise.
<i>OutDirLink</i>	Indicator variable equal to 1 if the director is an outside director of the company in question with affiliated links with the company and 0 otherwise. The IRRC treats as a linked director: someone “who is a former employee; is an employee of or is a service provider, supplier, customer; is a recipient of charitable funds; is considered an interlocking or designated director; or is a family member of a director or executive.” Definitions for RiskMetrics’ Directors Dataset, http://wrds.wharton.upenn.edu/ds/riskmetrics/dir_doc.shtml (last visited Apr. 20, 2009).
<i>PPill</i>	Indicator variable equal to 1 if a poison pill exists for the company in question (as measured by the IRRC for the year prior to the annual meeting date) and 0 otherwise.

- Prior Restat* Indicator variable equal to 1 if news relating to a financial restatement was first made public within two years prior to the meeting date (either in an SEC filing or through a public press release) and 0 otherwise.
- Prior SEC* Indicator variable equal to 1 if news relating to an SEC investigation or enforcement action was first made public within two years prior to the meeting date (either in an SEC filing or through a public press release) and 0 otherwise.
- Sdret* Standard deviation of returns for the company in question for the one-year period prior to the annual meeting date.
- Top5AbComp* Indicator variable equal to 1 if the total excess compensation for the CEO for the company in question is in the top 5 percent of the sample and 0 otherwise. We define Total Excess CEO Compensation as the difference between the Total CEO Compensation for the year prior to the meeting date (as provided by the Compustat Executive Compensation database) minus the Expected Total CEO Compensation. We calculate the Expected Total CEO Compensation by first estimating an OLS model as follows (following a model suggested to us by Martijn Cremers):
- $$\begin{aligned} \ln(\text{Total CEO Compensation}) = & \alpha + \beta_1 \ln(\text{market_cap}) \\ & + \beta_2 \text{Three_Year_Abnormal_Holding_Period_Return} \\ & + \beta_3 \text{Three_Year_Standard Dev. of Returns} \\ & + \beta_4 \text{Year_2006} + \text{Industry Effects} + \varepsilon \end{aligned}$$
- We then use the predicted Total CEO Compensation based on this model as the Expected Total CEO Compensation. Industry effects were based on two-digit SIC codes. *Abnormal_Holding_Period_Return* is defined as the difference between the holding period return and the value-weighted CRSP market index for the same period.
- Top5AbRet* Indicator variable equal to 1 if the abnormal return for the three-year period prior to the annual meeting date for the company in question is in the top 5 percent of the sample and 0 otherwise. The abnormal return is defined as the difference between the raw three-year holding period return for the company in question and the three-year holding period return for the CRSP value-weighted market index.
- VoteEJ* Indicator variable equal to 1 if EJ recommends a Withhold vote for the director in question and 0 otherwise.

2009]

DIRECTOR ELECTIONS

701

<i>VoteGL</i>	Indicator variable equal to 1 if GL recommends a Withhold vote for the director in question and 0 otherwise.
<i>VoteISS</i>	Indicator variable equal to 1 if ISS recommends a Withhold vote for the director in question and 0 otherwise.
<i>VotePG</i>	Indicator variable equal to 1 if PG recommends a Withhold vote for the director in question and 0 otherwise.
<i>Year06</i>	Indicator variable equal to 1 if the director recommendation is for 2006 and 0 otherwise (for 2005).

